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IN THE

Supreme Court of the United States

OCTOBER TERM—1950

No. 540

WASHINGTON GAS LIGHT COMPANY,
Petitioner,

against

VERNON V. BAKER,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT.

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Washington Gas Light Company prays that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered on December 21, 1950, affirming the order of the District Court which vacated and set aside an order of the Public Utilities Commission of the District of Columbia.

Opinions Below.

The opinion of the United States Court of Appeals for the District of Columbia Circuit (not yet officially reported) appears at R. 1041. The opinion of the District Court (not yet officially reported) appears at R. 10-18. The opinion of the Public Utilities Commission of the District of Columbia accompanying its order No. 3600, dated November 9, 1949, appears at R. 77-105.

Jurisdiction.

The judgment of the Court of Appeals for the District of Columbia Circuit was entered on December 21, 1950 (R. 1054). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code and Section 43-705 of the District of Columbia Code (1940), being part of the Act of March 4, 1913, 37 Stat. 979, as amended.

Questions Presented.

1. Can a reviewing court prescribe, as a matter of law under the "prudent investment theory", that a regulatory body must reduce the allowable earnings of a utility which converts to natural gas, either by elimination of actual dollar investment from the rate base or by reduction of rate of return?

2. Can a reviewing court properly substitute its judgment for that of a regulatory body as to the method to be used in determining reasonableness of utility rates?

3. To determine reasonable rates, must the regulatory body require new evidence as to the allowable rate of re-

turn where there is no disagreement as to the fairness of the rate of return previously established?

4. Can a reviewing court properly set aside the order of a regulatory body for lack of formal findings not prescribed by statute, when the opinion of the regulatory body clearly discloses the basis of its determination?

Statutes Involved.

The principal statutory provisions involved are:

D. C. Code (1940) §43-301:

> "Every public utility doing business within the District of Columbia is required to furnish service and facilities reasonably safe and adequate and in all respects just and reasonable. The charge made by any such public utility for any facility or services furnished, or rendered, or to be furnished or rendered, shall be reasonable, just, and nondiscriminatory. Every unjust or unreasonable or discriminatory charge for such facility or service is prohibited and is hereby declared unlawful. Every public utility is hereby required to obey the lawful orders of the commission created by chapters 1-10 of this title." (Mar. 4, 1913, 37 Stat. 977, ch. 150, §8, par. 2.)

D. C. Code (1940) §43-706:

> "In the determination of any appeal from an order or decision of the commission the review by the court shall be limited to questions of law, including constitutional questions; and the findings of fact by the commission shall be conclusive unless it shall appear that such findings of the commission are unreasonable, arbitrary, or capricious." (Mar. 4, 1913, 37 Stat. 989, ch. 150, §8, par. 66; Aug. 27, 1935, 49 Stat. 883, ch. 742, §2.)

Other pertinent statutes are set forth in the Appendix *infra*, p. 30.

Statement.

On July 14, 1949, Washington Gas Light Company (the Company) made application to the Public Utilities Commission of the District of Columbia (the Commission) for an emergency rate increase designed to produce additional operating revenues of $900,000 on an annual basis and to raise the Company's level of earnings up to a 5.34% rate of return (R. 67). After full public hearings the Commission on November 9, 1949 granted a lesser increase calculated to produce additional annual operating revenues of $750,000 on the basis of 1948 billings. On appeal by a consumer who had not participated in the hearings,* the District Court vacated the order of the Commission on the ground that certain items had been improperly included in the rate base as a matter of law.

The Court of Appeals affirmed the order of the District Court, but on entirely new and different grounds. It held that the Commission had discretion to include the disputed items in the rate base but that, if the Commission did so, this treatment must be offset in the rate of return. The Court of Appeals then prescribed a series of detailed inquiries and findings to be made by the Commission in arriving at a rate of return, apparently designed to force the Commission to lower the 6% rate already established by it.

The use by the Court of Appeals of the technique of dictating regulatory methods through requirements of additional findings is fully as stultifying to effective admin-

* The reference by the Court of Appeals to an adjournment of the Commission hearings "to afford the appellee and others the opportunity to prepare their opposition" (R. 1042) indicates that the Court of Appeals has overlooked the fact that appellee did not participate in the Commission hearings.

istrative action as the use by reviewing courts in former years of the technique of full judicial review, when the "present fair value" doctrine of rate-making was dominant.

Proceedings Below.

The principal issues in the proceedings before the Commission and in the appeals to the District Court and the Court of Appeals related to the effect upon the Company's rates of its change-over in 1947 from the distribution and sale of a mixed gas (a mixture of manufactured gas and natural gas) to the distribution and sale of straight natural gas. Prior to the change-over, the Company manufactured water gas at two plants known as East and West Stations, which was enriched with natural gas purchased from a non-affiliated company. The "mixed" gas thus produced was then distributed and sold by the Company. The change-over to natural gas required substantial expenditures by the Company to convert customers' appliances to the use of straight natural gas and required the abandonment of the West Station. The East Station was continued in use as a temporary standby plant (R. 80).

The Company's application to the Commission for a rate increase in July 1949 emphasized the urgency of prompt action on the relief requested in order to preserve the financial integrity of the Company (R. 67, 68). The public had benefited by the change-over to natural gas, since the cost of natural gas to the Company, after giving effect to the amortization of the extraordinary property losses and the cost of conversion of customers' appliances, was still 3% less in 1949 than the cost of the manufactured gas supply ten years before, in 1939 (R. 582, 594). However, this saving had been more than offset by heavy increases in the costs of maintenance and operation of the intricate distribution system of the Company and the costs

of providing necessary service in customers' homes and places of business. The steady increase in these expenses, principally labor costs, resulted in a serious decline in net operating revenues. In the short space of four years following World War II, during which the Company's investment in the public service increased, the net operating revenues of the Company declined almost 50%, from over $2,026,000 for the twelve months ended June 30, 1946 to about $1,106,000 for the twelve months ended May 31, 1949 (R. 585). The Company's rate of return earned during this period on its average investment declined from slightly over 6% to 3.38% (R. 585).

The Company's rates for gas service in the District of Columbia have been closely regulated by the Commission for many years. In the 29 years prior to this proceeding the Company's rates have been reduced many times and increased only once, 2¼%, in 1942 (R. 68). Since the Commission has only four major utilities in the District of Columbia to regulate, it is able to keep a representative at the office of the Company at all times and to maintain a constant supervision of the activities of the Company (R. 189).

Full public hearings were held on the Company's application in which a number of consumer interests participated, including counsel for the General Services Administration of the United States and Peoples Counsel for the District of Columbia. During the hearings all parties had ample opportunity to adduce testimony and cross-examine witnesses. The transcript of the record before the Commission comprises nearly 2,000 pages and 56 exhibits were introduced in evidence comprising over 100 pages of financial and statistical data.

The Commission tested the reasonableness of the proposed rates against a rate base computed upon the basis of the net amount of dollars actually invested by the Company in the public service after deducting all portions of the investment previously recovered by the Company either through depreciation or amortization. It accordingly included in the rate base (a) the unamortized portion of the Company's investment in the West Station (average age of such facilities at time of retirement in 1947—28 years) and (b) the unamortized portion of the cost of converting customers' appliances. The Commission ordered these costs to be charged off as deductions from operating revenues over a ten-year period, and also ordered the Company to depreciate the East Station at an accelerated rate over a ten-year period.

The District Court based its judgment upon the conclusion that it was an error of law for the Commission to include the Company's investments in abandoned property and conversion costs in the rate base, since neither investment remained in the form of physical property used and useful in the public service. The Court of Appeals rejected the reasoning of the District Court recognizing that "the composition of the rate base falls within the province of the Commission under the doctrine of the *Hope* case" (R. 1047) and that "the 'used and useful' standard is no necessary part" of the prudent investment theory (R. 1048). However, the Court of Appeals reached the same result as the District Court by the simple expedient of requiring the inclusion of abandoned property in the rate base to be "offset" in the rate of return, and holding the record and findings to be inadequate with respect to (a) rate of return and (b) the question of whether the investor or the consumer should bear the risk of obsolescence of property. The Court

of Appeals did not disturb the Commission's treatment of conversion costs or review certain other questions presented to the District Court.

Evidence as to Rate of Return.

The evidence introduced by the Company in the proceedings before the Commission showed that the return received by it on its average investment for the twelve months ended May 31, 1949, amounted to 3.38% (Exhibit 11, R. 585). The Commission's staff of accountants made a detailed examination of the Company's exhibits and introduced their own exhibits which differed from the Company's exhibits both as to amount of investment and revenues (Exhibits 19-21, R. 603-607). Even upon the basis of the computations made by the Commission's witness, however, the return realized by the Company for the twelve months ended May 31, 1949, amounted to only 3.70% on its average investment. The rate increase of $900,000 requested by the Company would have increased the rate of return earned for the twelve months ended May 31, 1949, after making an adjustment to reflect normal winter temperatures and other changing conditions, to 5.34% according to the Company and to 5.75% according to the Commission's witness (Exhibit 17-A, R. 597, 204).

On the question of rate of return, the Commission's witness testified that the Commission in 1944 had fixed a rate of return of 6% as an independent determination of a reasonable rate of return (not limited to the sliding scale arrangement then in effect), based upon a study of the cost of capital to the Company at that time (R. 209). A copy of Order No. 2827 of the Commission making this determination and its accompanying opinion is included in the record

(R. 767-773). Also in the record is Order No. 2944 of the Commission, and its accompanying opinion, dated August 29, 1945, fixing 6% as the rate of return to continue until further order of the Commission* (R. 773-778). This opinion refers to the testimony of the Commission's witness that "a primary rate of return of 6% should remain in effect until further order of this Commission, so that it would not again be necessary to review this question in the immediate future unless changed conditions indicate that such a review is warranted" (R. 775).

The Company's application for emergency relief did not request an increase sufficient to bring it up to the 6% rate of return previously established, and no participant in the proceeding sought to challenge the fairness of the 6% rate of return previously established. Under these circumstances the Commission did not require presentation of any new cost of money study.

It was, of course, for the Commission, not the Court of Appeals, to decide whether there had been such a change in economic conditions since 1945 as to require a new study of rate of return. The Commission is an expert body concerned with utility regulation. As such, it not only had detailed financial and statistical information about the Company, which is in the record, but also it was in a position to know the general increase in cost of money as indicated by yields on stocks of comparable utilities which had occurred

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* The Court of Appeals ignored this order and the 1944 order and erroneously stated that the most recent rate proceeding was in 1943 fixing 5¾% as a fair rate of return (R. 1046, Footnote 24). (The 1943 order referred to was set aside in 1944. *Washington Gas Light Co.* v. *Public Util. Com'n*, 55 F. Supp. 627.) This error may have resulted from the fact that in the instant case the question of fair rate of return was not properly before the Court of Appeals and had not been argued.

between 1945 and 1949.* During that four year period the Company had appeared before the Commission on six separate occasions, requesting the approval by the Commission of all types of security issues. In each instance the Commission investigated the cost of capital resulting from the issuance of each type of security, and approved the requested issue.

Evidence as to Risk of Obsolescence of Property.

The Court of Appeals was primarily concerned with whether the consumer or investor should bear the risk of obsolescence of the property devoted to public service. This question was fully explored in the proceedings before the Commission. The witness for the General Services Administration testified that the change-over to natural gas was one of the uncertainties which are a hazard of the manufactured gas business and are provided for in the return permitted. He stated that the "only justification for a 6 per cent. rate of return on investment in a gas company as compared to the 3 per cent. return on a government bond is that the former is subject to certain hazards and uncertainties and the latter is not". He urged his view that investors had been fully remunerated in the past for this hazard and concluded by proposing an "equitable and practical solution" to the effect that the investment in an abandoned plant should be amortized as a deduction from operating

* As stated in the Joint Report of Committees of American Gas Association and Edison Electric Institute "Financing Utility Capital Requirements" 1949: "Rising trends are shown by a tabulation of dividend yields at the offering prices of utility common stocks issued from 1946 to June 30, 1949 (Table IV-9). From dividend yields of 4% to 4½% in 1946, it became necessary in 1948 and early 1949 to offer utility common stocks at from 6% to 7½%, with some at even higher yields" (p. 35). The S. E. C. market price index of utility common stocks shows a drop of 18% from May 1945 to December 1948 (op. cit. 57).

revenues but not included in the rate base (R. 314-315). He conceded, however, that if the abandonment of the West Station could have been foreseen, it should have been provided for by depreciation accruals (R. 324).

The Executive Accountant and Auditor for the Commission testified that the Company's provisions for depreciation had been prescribed by the Commission, and that the Company had contended for many years, since 1913, that the allowance for depreciation permitted by the Commission had been inadequate (R. 281). The Commission's witness further testified that the inadequate provision for depreciation in the past had resulted in a lower cost of service and, therefore, "an equitable balancing of the interests of investors and consumers, in my opinion, requires that this item be treated the same as any other unrecovered investment" (R. 497-498). The Commission's witness also testified that if the rate base were to be lessened in accordance with the theories of the witness for the General Services Administration a higher rate of return would have to be provided to meet the capital costs of the business (R. 529).

Opinion and Order of the Commission.

Against this background of testimony and evidence the Commission issued its opinion and order on November 9, 1949 (R. 77-117). The Commission reviewed the conflicting testimony as to whether the abandonment of property was a hazard of the business provided for in the 6% rate of return allowed the Company or whether, since the deficiency in depreciation reserve was occasioned by inadequate depreciation accruals generally prescribed and limited by the Commission, the investor should be permitted the ultimate recovery of his investment. The Commission concluded that if it had known well in advance that the manu-

factured gas plant would be retired in 1947 "sufficient depreciation would have been allowed to provide for the retirement of such property", and that "the exclusion of this item from the rate base would deprive investors of a return on an investment originally made to furnish utility service which, by reason of inadequate depreciation accruals, was not fully recovered at the time of abandonment" (R. 89).

The Commission reviewed the testimony as to the rate of return currently earned by the Company on its investment, and pointed out that a return of less than 4% is "obviously inadequate to maintain the Company in a sound financial position" (R. 103). The Commission stated that an increase in rates "appears necessary to maintain the Company in a sound financial position" (R. 103). The Commission reviewed the testimony of both Company and Commission witnesses as to whether the requested increase of $900,000 would have increased the return earned during the twelve months ended May 31, 1949 to a rate of 5.34% or to 5.75% (R. 100, 102). The Commission pointed out the possible effect upon rate of return of increased volume of business in the future, and concluded that rate schedules calculated to produce $750,000 when applied to the sales of gas in the District of Columbia during the calendar year 1948, "will provide the Company with a reasonable return in the immediate future and, at the same time, will confine the burden of consumers to the minimum necessary under the circumstances" (R. 104). It may be noted that under the new rates the monthly bill of the average domestic customer who uses gas for cooking and water heating and refrigeration was increased by only 24¢ from $3.31 to $3.55 (R. 104, 551). The Commission then made the ultimate finding that the rates specified in the order attached to its opinion "are just, reasonable and nondiscriminatory

and will permit the Company to earn a fair return upon its investment devoted to public service and maintain its financial integrity" (R. 105).

It was against this background that the Court of Appeals held that additional findings should have been made by the Commission as to rate of return and that, if abandoned property is included in the rate base, the Commission must require an "offset" in the rate of return.

Specification of Errors to Be Urged.

The Court of Appeals erred:

1. In requiring the Commission as a matter of law under the prudent investment theory to reduce the allowable earnings of the Company either by elimination of actual dollar investment from the rate base or by reduction of rate of return.

2. In substituting its judgment for that of the Commission as to the method to be followed in testing the reasonableness of utility rates.

3. In holding the Commission powerless to test the reasonableness of rates on the prudent investment theory, unless

(a) The Commission required new evidence to be introduced bearing on the allowable rate of return previously established by it;

(b) The Commission required evidence to be introduced as to whether past investors assumed the risk of obsolescence of property or, if such risk was not assumed, undertook the risk that at the time of retirement of obsolete property the reserve for depreciation might prove inadequate; and

(c) The Commission required evidence to be introduced as to whether the past earnings of the Company sufficiently exceeded a fair rate of return to compensate investors for past inadequate depreciation changes.

4. In holding that the record and findings of the Commission were inadequate with regard to rate of return, abandoned property and standby plant.

5. In disregarding the provisions of Section 43-704 of the District of Columbia Code (1940) designed to prevent the reversal on appeal of orders of the Commission on grounds not specified in an application to the Commission for reconsideration.

Reasons for Granting the Writ.

1. The Review of the Decision of the Court of Appeals Is of Nation-Wide Importance.

The most important development in the gas industry today is the advent of natural gas and the opportunity afforded to utilities which now use manufactured gas to convert to natural gas. Many cities and towns throughout the United States are now in the process of changing over to natural gas. Conversion to natural gas almost inevitably involves the abandonment of a part of the existing facilities of the utility before the dollar investment in these facilities has been recovered through depreciation accruals. The decision of the Court of Appeals serves notice upon utilities generally that to take the step of conversion to natural gas must result in reduction of allowable earnings either through elimination of dollar investment from the

rate base or through reduction in rate of return. The Court of Appeals said:

> "• • • Although we think the *Hope* doctrine precludes us from forbidding the Commission to include abandoned property in the rate base, we are convinced that protection of the consumer interest requires that such treatment of abandoned property be offset in the rate of return" (R. 1050).

This decision casts a shadow on the economics of change-over to natural gas, and requires a utility to penalize its investors if it wishes to obtain for its consumers the benefits of natural gas.

The particular method which the Court of Appeals has prescribed is undesirable and unfair. The importance of the decision of the Court of Appeals, however, does not lie in the undesirability of the method which it prescribes, but in the fact that it strikes directly at the doctrine of *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591 (1944) that the reviewing court exceeds its power when it attempts to prescribe the method to be followed by the regulatory body. Under the Court of Appeals' decision, the reviewing court, while paying lip service to the doctrine of the *Hope* case, can vacate the order of the regulatory body if the court disagrees with the economic merits of the rate base adopted by the Commission simply by requiring an "offset" in the rate of return. The Court of Appeals has phrased its requirements as to method in terms of requirements as to findings (a) as to matters not in issue and (b) as to historical matters impossible of determination. The passage from the Court's opinion quoted above, however, clearly reveals that the Court of Appeals used the technique of requiring findings as a tool to coerce the Commission to adopt the economic theories of the Court of Appeals.

The decision of the Court of Appeals points out that the applicable statute of the District of Columbia "invests the District of Columbia Public Utilities Commission with the same broad authority as is possessed by the Federal Power Commission under the Natural Gas Act" (R. 1043). The decision is thus of general importance. It suggests a means by which any order of a regulatory body may be vacated by a reviewing court merely by finding some area in which the regulatory body has made no subsidiary "finding".

It is always possible for a reviewing court to pore over the record and findings in a rate proceeding and find some factual question as to which more evidence could have been introduced or fuller findings made. No two administrative bodies and no two courts would conduct a rate inquiry in precisely the same way, but if administrative rate making is to be effective the reviewing court must respect the area of discretion of the administrative body. As stated by the chief counsel for the Wisconsin Public Service Commission:

> "Utility rate making will never be free from the delay and expense, and sometimes the futility, which now attends it, unless there is a recognition, both by regulatory agencies and by the courts which review their orders, that rate making is essentially an administrative and not a judicial process. *Rates cannot be expeditiously or efficiently made if every single fact which pertains to their reasonableness must be in the record in the proceeding in which they are made.* Reviewing courts should also concede that rates, determined by regulatory agencies, cannot properly be set aside upon judicial review upon anything less than a showing that the facts avowedly relied upon are contrary to the evidence." (Emphasis supplied) (H. T. Ferguson: "Why Is a Rate Base?" 39 Public Utilities Fortnightly, 811, 816 (1947).)

The applicable statute of the District of Columbia has sought to guard the Commission against action by a reviewing court based on grounds not urged before the Commission. Section 43-704 of the District of Columbia Code (1940), provides for the filing with the Commission by any person affected by its decision of "an application in writing requesting a reconsideration of the matters involved, and stating specifically the errors claimed as grounds for such reconsideration". The statute then provides:

> "No public utility or other person or corporation shall in any court urge or rely on any ground not so set forth in said application." (Appendix, page 30.)

A similar provision in the Natural Gas Act, 15 U. S. C. A. §717c(a), was quoted in the concurring opinion in this Court in *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission,* 324 U. S. 635 (1945). In this case Justices Stone, Roberts, Reed and Frankfurter concurred in the opinion of the Court "for the following reasons only":

> "Petitioners did not raise objections in their application for rehearing to the Commission to the inclusion of their producing and gathering facilities in the rate base. By §19(b) of the Natural Gas Act: 'No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do.' No reason appears for the failure of petitioners here to make objection on rehearing to the inclusion of the production and gathering facilities in the rate base." (pages 650-651)

The Court of Appeals ignored the provisions of the District of Columbia Code. It vacated the order of the

Commission on grounds which had not been urged before the Commission or included in any application for reconsideration. It did not even remand the proceedings to the Commission to permit the Commission to make the inquiries and utter the formula required by the Court of Appeals. Instead it directed the Company to distribute to ratepayers the amount which it had collected attributable to the rate increase and relegated the Company to the old rates which the Commission had found inadequate.

The Court of Appeals has introduced a new technique for exercising indirectly a type of review which it concedes this Court has forbidden it to exercise directly. It is only in the last decade that rate regulation has moved away from the type of judicial review which involved "hearings and law suits so protracted as to frustrate rate regulation" (*St. Joseph Stock Yards Co.* v. *United States,* 298 U. S. 38 (1936)). The effect of the decision of the Court of Appeals is to place regulatory bodies once again on notice that, regardless of the willingness of all the parties to a proceeding to avoid protracted inquiries into matters where there is no disagreement, unless every issue is canvassed which a reviewing court might regard as important, the regulatory body's order may be summarily set aside.

2. The decision of the Court of Appeals is in conflict with the principle established by this Court that, within the limits of procedural due process, the regulatory body is free to choose its own method of determining reasonableness of rates.

In *Federal Power Commission* v. *Natural Gas Pipeline Co.,* 315 U. S. 575 (1942), Chief Justice Stone made the following statement:

> "The Constitution does not bind rate-making bodies to the service of any single formula or com-

bination of formulas. Agencies to whom this legislative power has been delegated are free, within the ambit of their statutory authority, to make the pragmatic adjustments which may be called for by particular circumstances. *Once a fair hearing has been given, proper findings made and other statutory requirements satisfied, the courts cannot intervene in the absence of a clear showing that the limits of due process have been overstepped.* If the Commission's order, as applied to the facts before it and viewed in its entirety, produces no arbitrary result, our inquiry is at an end" (p. 586). (Emphasis supplied.)

In their concurring opinion in the *Natural Gas Pipeline* case, Justices Black, Douglas and Murphy said:

"* * * *In view of these provisions, we do not think it is permissible for the courts to concern themselves with any issues as to the economic merits of a rate base.* The Commission has a broad area of discretion for selection of an appropriate rate base.* * *

"It is not the function of the courts to prescribe what formula should be used * * *. The decision in each case must turn on considerations of justness and fairness which cannot be cast into a legalistic formula. *The rate of return to be allowed in any given case calls for a highly expert judgment. That judgment has been entrusted to the Commission. There it should rest*" (pp. 606-607). (Emphasis supplied.)

Again in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591 (1944), this Court said:

"Under the statutory standard of 'just and reasonable' it is the result reached not the method employed which is controlling * * * It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. *The fact that the method employed*

> *to reach that result may contain infirmities is not then important.* Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged. It is the product of expert judgment which carries a presumption of validity. And he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences" (p. 602). (Emphasis supplied.)

Under these decisions as long as the "procedural safeguards" of due process and "rudiments of fair play" are observed, the Commission is free to determine for itself the method to be employed in testing reasonableness of rates. The applicable statute of the District of Columbia provides that rates must be "reasonable, just, and nondiscriminatory" (p. 3, *supra*) but does not prescribe any formula which must be followed by the Commission in making its determination of reasonableness. The Commission chose to test reasonableness of rates against a rate base computed upon the basis of the dollars actually invested by the Company in the public service which had not been returned to the Company through depreciation or amortization charges. In so doing it followed the method stemming from the famous concurring opinion of Mr. Justice Brandeis in 1923 in the *Southwestern Bell Telephone Co.* case where it was pointed out that

> "The thing devoted by the investor to the public use is not specific property, tangible and intangible, but capital embarked in the enterprise. Upon the capital so invested the Federal Constitution guarantees to the utility the opportunity to earn a fair return" (*Southwestern Bell Tel. Co.* v. *Pub. Serv. Com'n.*, 262 U. S. 276, 290 (1923)).

As further pointed out by Mr. Justice Brandeis, under the prudent investment theory

> "The cost of a scrapped plant is carried as part of the investment on which a return must be paid unless and until it has been retired, that is fully paid, out of the depreciation reserve" (*Pacific Gas & Electric Co.* v. *San Francisco,* 265 U. S. 403, 425) (1924).

The Commission thus included in the rate base the unamortized portion of the Company's investment in its manufactured gas plant. The Court of Appeals recognized that the Commission was entitled to use dollar investment as the test of reasonableness of rates, and further recognized that the "used and useful standard" was no necessary part of this test, but the Court then rendered meaningless its apparent recognition of the Commission's discretion, by saying that inclusion of abandoned property in the rate base must be "offset in the rate of return" (R. 1050). This amounts to giving the Commission the latitude as to method required by the *Hope* case with one hand and taking it away with the other. The Court here clearly was concerned with the "economic merits of a rate base" in violation of the injunction in the *Natural Gas Pipeline* case.

The Court of Appeals attempted to buttress its decision by charging that the record and findings were inadequate as to rate of return and risk of obsolescence. The state of the record as to these matters has been reviewed at pages 8 to 11 above. There is no real disagreement between the Court of Appeals and the Commission as to basing rate of return on a cost of money study. The Commission fixed its 6% rate of return on the basis of a cost of money study by a prior order which the Court of Appeals apparently overlooked. As will be shown below, procedural due

process did not require the Commission to make another investigation of cost of money where no participant in the proceeding questioned the fairness of the 6% rate of return. The basic difference between the Court of Appeals and the Commission is that the Court of Appeals would not accept the rate of return indicated by a cost of money study, but would adjust it downwards to a point below the cost of money depending upon the results of a historical review of the past earnings of the Company. The Court of Appeals would substitute for the objective determination of cost of money, a subjective determination of rate of return based on a historical guess as to what elements of risk past investors believed they were assuming.

The Court of Appeals prescribed that the Commission could not include abandoned property in the rate base for the purpose of testing reasonableness of rates unless it made the following specific inquiries:

(a) The Commission must inquire whether the risk of obsolescence was in the past regarded as a proper element of depreciation. The Court of Appeals reasons that, if not, it must be a risk for which investors have already been compensated in the rate of return.

(b) The Commission must inquire whether, even if the risk of obsolescence was properly regarded as an element of depreciation, the past investors assume the risk that the reserve for depreciation might prove inadequate. The Court of Appeals reasons that past investors took this risk because under "fair value" rate regulation property "not used and useful" was omitted from the rate base.

(c) The Commission must inquire whether earnings in the past sufficiently exceeded a fair rate of return to compensate investors for inadequate depreciation charges.

These inquiries prescribed by the Court of Appeals clearly relate to "method", not to "end result". Moreover, such inquiries would be peculiarly burdensome, time-consuming and unrealistic in view of the changes that have occurred in rate-making standards. It was only in 1946 that it was finally established by the decision of the Court of Appeals in *Potomac Electric Power Company* v. *Public Utilities Commission*, 158 F. 2d 521 (1946) (cert. den. 331 U. S. 816) that rate-making in the District of Columbia does not depend upon present fair value. The hypothetical investor into whose state of mind the Court of Appeals has directed inquiry would presumably have believed, up until very recent years, that he was entitled to a return on the present fair value of the utility's property used and useful in the public service. The investor's risk that property might be prematurely abandoned because of obsolescence was more than offset by the increase in fair value of property retained in the rate base, resulting from steadily mounting costs and the declining value of the dollar. If the investor were sufficiently clairvoyant to foresee the shift in regulation to a base of dollars invested, rather than present fair value, he presumably would have anticipated also that dollars invested in property prematurely abandoned would continue in the rate base until returned through amortization. He would not have expected to receive the disadvantages of both theories and the benefits of neither.

Similarly to require the Commission to review the past earnings of the Company to determine whether they exceeded the fair rate of return is to pose a fruitless and almost impossible task. The first question is one of definition of a fair rate of return. If in past years a fair rate of return is determined upon the present fair value theory of rate-making then predominant, the Commission would have to estimate reproduction cost of property for each of

the past years and also to make the detailed inquiries as to cost of money, etc. prescribed by the Court of Appeals as bearing on rate of return.

The Court of Appeals, in prescribing the detailed inquiries to be made by the Commission, has clearly invaded the province of the Commission in direct conflict with the principles established by this Court. The suggestion of endless further inquiries which might have been made by the Commission, but which neither the Commission, the Company nor any consumer participant in the proceedings sought to make, is not the "convincing showing" that the end result of the rate order is unreasonable which "he who would upset the rate order under the Act carries the heavy burden of making". (*Federal Power Commission* v. *Hope Natural Gas Co., supra.*)

3. The decision of the Court of Appeals is in conflict with the principle established by this Court that procedural due process does not require production of evidence as to matters not in issue.

In *Railroad Commission* v. *Pacific Gas & Electric Co.*, 302 U. S. 388 (1938), Chief Justice Hughes analyzed the requirements of procedural due process as follows:

> "The right to a fair and open hearing is one of the rudiments of fair play assured to every litigant by the Federal Constitution as a minimal requirement. Ohio Bell Telephone Co. *v.* Public Utilities Commission, 301 U. S. 292, 304, 305. There must be due notice and an opportunity to be heard, the procedure must be consistent with the essentials of a fair trial, and the Commission must act upon evidence and not arbitrarily. * * *
>
> "The complaint is not of the absence of these rudiments of fair play but of the method by which the Commission arrived at its result. As to this a fundamental distinction must be observed. While a

> fair and open hearing must be accorded as an inexorable safeguard, we do not sit as an appellate board of revision but to enforce constitutional rights. San Diego Land & Town Co. *v.* Jasper, 189 U. S. 439, 446. When the rate-making agency of the state gives a fair hearing, receives and considers the competent evidence that is offered, affords opportunity through evidence and argument to challenge the result, and makes its determination upon evidence and not arbitrarily, the requirements of procedural due process are met, and the question that remains for this Court, or a lower federal court, is not as to the mere correctness of the method and reasoning adopted by the regulating agency but whether the rates it fixes will result in confiscation" (393-394).

The requirements of procedural due process as outlined by Chief Justice Hughes were clearly met in the proceedings before the Commission. There was a fair and open hearing. There was due notice and an opportunity to all participants to introduce evidence and to produce and cross-examine witnesses.

The Commission did not reject any evidence proffered by any participant to the proceeding bearing on any of the questions raised by the Court of Appeals. It is submitted that where a fair hearing is held the Commission is not deprived of its power to determine reasonableness of rates by the failure on the part of the participants in the proceeding to produce evidence. There are, of course, many cases where decisions of administrative bodies have been vacated on the ground of improper refusal to receive or to consider relevant evidence. It is believed that the decision of the Court of Appeals is unprecedented in vacating the decision of a regulatory body for lack of evidence on a point which no party sought to question or to test or to make the subject of new evidence.

There are many precedents for the fixing of rates by a regulatory body without any hearing except to the extent such hearing is requested by the utility affected. Thus in *United States* v. *Illinois Cent. R. Co.*, 291 U. S. 457 (1934) this Court upheld the provision of the Inland Waterways Corporation Act authorizing the Interstate Commerce Commission to fix joint water and rail rates without a hearing except upon receipt of a complaint as to any order. This is in direct conflict with the principle of the Court of Appeals that the regulatory body is powerless, even though all parties are in agreement, unless all the findings prescribed by the Court of Appeals are made and evidence introduced. The distinction between the procedure to be followed by a regulatory body on a contested issue of fact and that to be followed where there is no real controversy was outlined as follows by the Wisconsin Supreme Court in *Wisconsin Telephone Co.* v. *Public Service Commission*, 232 Wis. 274, 287 N. W. 122, cert. den. 309 U. S. 657:

> "• • • What must always be borne in mind is that there is a wide difference between what may be done by way of increasing or decreasing rates upon the application of the utility or decreasing rates against the protest of the utility. When rates are increased upon the application of the utility, the Commission consents for the public and the resulting order is in effect a consent order. When rates are decreased upon application of the utility a like consent order results if the Commission approves the decrease. The statute prohibits an increase or decrease of rates without the consent or approval of the Commission. When, however, the utility objects and an issue is thus raised, the considerations which then govern the action of the Commission are entirely different. The Commission must then proceed with full regard to the statutory and constitutional rights of the utility." (p. 306)

The same basic principle is involved in the statement of Chief Justice Stone in *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575 (1942), that:

> "* * * The right to a full hearing before any tribunal does not include the right to challenge or rely on evidence not offered or considered. * * * " (p. 584)

4. The decision of the Court of Appeals is in conflict with the principle established by this Court that the requirement of findings is met if the opinion of the regulatory body clearly sets forth the basis of its determination.

This Court has consistently held that, where specific formal findings are not prescribed by statute and are not jurisdictional requirements, the test of adequacy of findings is met if the opinion of the administrative body shows the reviewing court what the administrative body has really determined and what path it has followed. In *Colorado Interstate Gas Co.* v. *Federal Power Com'n*, 324 U. S. 581 (1945), Mr. Justice Douglas applied this test in rejecting a contention that findings of the Federal Power Commission on allocation of costs were inadequate. He said:

> "* * * The findings of the Commission in this regard leave much to be desired since they are quite summary and incorporate by reference the Commission's staff's exhibits on allocation of cost. But the path which it followed can be discerned. And we do not believe its findings are so vague and obscure as to make the judicial review contemplated by the Act a perfunctory process * * *" (p. 595).

In *City of Yonkers* v. *United States*, 320 U. S. 685 (1944) this Court set aside an order of the Interstate Commerce Commission on the grounds of absence of requisite jurisdictional findings. The general principles applicable to review of findings of administrative agencies were dis-

cussed in the dissenting opinion of Mr. Justice Frankfurter as follows:

> "* * * But courts have also spoken of the need of findings as the basis of validity of an order by the Interstate Commerce Commission in the absence of a Congressional direction for findings. The requirement of findings in such a context is merely part of the need for courts to know what it is that the Commission has really determined in order that they may know what to review.
>
> * * * * * *
>
> The nub of the matter regarding the requirement of findings, where the formal making of them is not legislatively commanded, is indicated in *United States* v. *Louisiana,* 290 U. S. 70. Reviewing the validity of the Commission's order is the serious business of sitting in judgment upon a tribunal of great traditions and large responsibility. An order of the Commission should not be viewed in a hypercritical spirit nor even as though *elegantia juris* were our concern. We should judge a challenged order of the Commission by, 'the report, read as a whole,' 290 U. S. *supra* at page 80, and by the record as a whole out of which the report arose" (p. 695).

The findings and opinion of the Commission, read as a whole, give a perfectly clear picture of the path which the Commission followed in reaching its ultimate findings that the rates specified in its order "are just, reasonable and non-discriminatory". The Commission specifically referred to the question of whether "the rate of return of 6% allowed the Company" was intended to compensate the Company for the hazard of the abandonment of property or whether, in view of inadequate depreciation accruals prescribed by the Commission in the past, the Company should be entitled to recover its investment (R. 88). In

effect, both in the proceedings before the Commission and in the Commission's findings and opinion, the question considered was:

> "Assuming the 6% rate of return allowed the Company, should abandoned property be included in the rate base?"

The Court of Appeals merely says that the Commission should have phrased the question as follows:

> "Assuming the abandoned property in the rate base, should the rate of return be fixed at 6%?"

It is submitted that an order of a regulatory body should not be made dependent as to its validity upon its manner of expression of some prescribed formula, and should not be vacated by a play on words.

Conclusion.

For the reasons stated, it is respectfully submitted that this petition for a writ of certiorari should be granted.

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February, 1951.

APPENDIX.

D. C. Code (1940) §43-704

> "* * * Any public utility or any other person or corporation affected by any final order or decision of the commission may, within thirty days after the publication thereof, file with the commission an application in writing requesting a reconsideration of the matters involved, and stating specifically the errors claimed as grounds for such reconsideration. No public utility or other person or corporation shall in any court urge or rely on any ground not so set forth in said application. * * *" (Mar. 4, 1913, 37 Stat. 988, ch. 150, §8, par. 64; Aug. 27, 1935, 49 Stat. 882, ch. 742, §1.)

D. C. Code (1940) §43-1003

> "The provisions of chapters 1-10 of this title shall be interpreted and construed liberally in order to accomplish the purposes thereof, and where any specific power or authority is given the commission by the provisions of chapters 1-10 of this title the enumeration thereof shall not be held to exclude or impair any power or authority otherwise in chapters 1-10 of this title conferred on said commission. The commission hereby created shall have, in addition to the powers in chapters 1-10 of this title specified, mentioned, and indicated all additional, implied, and incidental power which may be proper and necessary to effect and carry out, perform, and execute all the said powers herein specified, mentioned, and indicated. A substantial compliance with the requirements of chapters 1-10 of this title shall be sufficient to give effect to all the rules, orders, acts, and regulations of the commission, and they shall not be declared inoperative, illegal, or void for any omission of a technical nature in respect thereto. * * *" (Mar. 4, 1913, 37 Stat. 993, ch. 150, §8, par. 92.)

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CHARLES ELMORE CROPLEY

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1950

No. 548

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA,

Petitioner,

v.

VERNON V. BAKER,

Respondent

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT.

To the Honorable, the Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

Your petitioner, the Public Utilities Commission of the District of Columbia (the Commission), respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered December 21, 1950, in the above entitled cause, and represents unto your Honors:

Opinions Below

The Opinion of the United States Court of Appeals for the District of Columbia Circuit is not yet officially reported, but may be found at R. 1041. The Opinion of the United States District Court for the District of Columbia is not reported but is printed in the Record at pages 10-18. The Findings and Opinion and Order of the petitioner are found at pages 77-117 of the Record.

Jurisdiction

The judgment of the United States Court of Appeals for the District of Columbia Circuit was entered on December 21, 1950 (R. 1054). The jurisdiction of this Court is invoked under Title 43, Section 705, of the District of Columbia Code, 1940 Edition (49 Stat. 883) and under Section 240(a) of the Judicial Code.

Questions Presented

The questions presented are:

1. May the lower Court vacate a rate order without considering and without determining whether the total effect of the rate order is unjust and unreasonable?

2. May the lower Court vacate and remand to the Commission a rate proceeding with instructions to substitute the Court's judgment as to (1) the method of measuring a component of the rate base, (2) the method of determining the rate of return to be allowed in this proceeding and "so far as the future is concerned", and (3) the kind of investigation to be conducted, and (4) require the Commission to deduct a reserve requirement from the original cost of property in establishing the rate base instead of the book reserve for depreciation?

3. May the lower Court set aside a rate order which fixed

the rate base at the original cost of property minus the book reserve for depreciation, on the ground that "the record contains no evidence as to whether earnings during the life of this property sufficiently exceeded the fair rate of return to compensate investors for the inadequate depreciation charges"?

4. May the lower Court set aside a rate order increasing rates to produce a rate of return of less than 5¾% on the prudent investment or unrecovered cost, when the utility's rate of return had been declining over a period of several years and, for the test year, had declined to 3.7%, on the ground that the Commission did not make an independent investigation in the instant proceeding to determine a proper rate of return to be allowed, in spite of the fact the Commission found, after investigation predicated upon the cost of capital, that 6% was a fair rate of return to be allowed the utility "until further order of the Commission"?

5. May the lower Court set aside a rate order which included in the prudent investment rate base the undisputed unrecovered investment in standby production plant being amortized on a ten-year basis, on the ground that there is no proof in the record that the rate of return allowed during the useful life of the said property did not include an element for the risk of abandonment?

6. May the lower Court vacate a rate order on issues raised (but not decided) by the lower Court which were not raised by the application for reconsideration nor by the petition of appeal and which could not under the statute be urged or relied upon by the complainant "in any court" without first raising such issues in (1) his application for reconsideration of the rate order and (2) his petition of appeal, when complainant admitted "that the facts are as stated by the Commission in its report"?

Statute Involved

Pertinent provisions of the statute involved are incorporated in the appendix of this petition.

Statement of the Matter Involved

On July 14, 1949, Washington Gas Light Company (the Company) filed an application with the Public Utilities Commission of the District of Columbia (the Commission) for an emergency increase of its rates to produce additional operating revenues of $900,000 in the aggregate on an annual basis. The rates then in effect were established on October 13, 1942. After notice and formal public hearings, the Commission denied the increase requested, but allowed an increase in rates which would produce $750,000 additional revenue when applied to the volume of gas sold in the District of Columbia during the calendar year 1948.

The record shows that an increase in operating revenues of $900,000 on an annual basis for the test year ended May 31, 1949, after adjustment for normal temperature conditions, would have produced a rate of return of 5¾% on the rate base found by the Commission for the test year (R. 103). The increase allowed will result in a return of less than 5¾%.

Upon appeal by the respondent from the Commission's order, the United States District Court for the District of Columbia (District Court) vacated and set aside the Commission's order because of the method used by the Commission in arriving at the rate base. Upon appeals by the Commission and the Company from that decision, the Court of Appeals affirmed the decision of the District Court, but on different grounds.

A more detailed statement of the proceedings before the lower Courts and the Commission follows.

Decision of the District Court

The respondent did not question any of the facts of record or the findings of the Commission. His petition of appeal alleged that the Commission erred "as a matter of law" in including in the rate base the unrecovered cost of property abandoned and to be abandoned because of conversion to the sale of straight natural gas and the unrecovered cost of adapting customers' appliances to the use of natural gas, and in amortizing the unrecovered cost of abandoned property, the conversion cost, and the standby plant at East Station on a ten-year period (R. 2-3). The petition of appeal raised no question as to the rate of return used by the Commission or the amount of the book reserve for depreciation.

The respondent admitted in the District Court "that the facts are as stated by the Commission in its report. We contend that they are errors of law committed by the Commission" (R. 23). He said:

> "With respect to the findings of fact, we do not question any of the basic findings of fact of the Commission. It is not necessary for Your Honor to peruse this tremendous record which counsel has showed you." (R. 57).

The District Court held that the Commission was in error as "a matter of law" in including in the prudent investment rate base the unrecovered cost of the abandoned property and the unrecovered cost of adapting customers' appliances to the use of straight natural gas (R. 16). It vacated and set aside the Commission's order because of the method by which the rate base was determined. The Court made no finding, whether the total effect of the rate order was unjust and unreasonable in its consequences.

The District Court held that the decision in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S.

591, did not, in its opinion, have "anything in it which controls in any way the action of the court in this case" (R. 11).

The District Court made no findings as to the result or total effect of the Commission's order, as shown by the following statement from the Court's opinion:

> "The Court is not passing upon the question as to whether or not this action of the Commission provides more income to the public utility than it should be entitled to. What the Court is attempting to say is that the matter should be approached not arbitrarily or cynically, because that only leads to bad methods; but it should be approached in the proper way.
>
> "If the utility can demonstrate to the Public Utilities Commission that they are not receiving a proper income, that the investors are not being properly treated, that they are not making a decent living, then the Commission has a perfect right to raise the cost of gas to the consumer. But, they should do it in a legal manner, and not in an arbitrary manner." (R. 14)

In answer to a statement that a different method could have been followed by the Commission by eliminating abandoned property from the rate base and increasing the rate of return to 6½% or 7%, the Court said:

> "Wouldn't that have been better than to drag in this stuff that may plague the community for all years to come?" (R. 42)

The Court further said:

> "It seems to me that a finding based upon these two items [abandoned property and conversion costs], if it is supported by the courts, would plague this jurisdiction and other jurisdictions for a great many years. I do not see any reason why, if it is necessary to bring more income in, the Public Utilities Commission could

not simply say so in plain English language and allow them to raise the rates." (R. 43)

* * * * * * *

"They [the Company] may not be making enough money. I do not know a thing about that. I have no information about it, and I have no means of getting information about it. But, what I am suggesting is this possibility that if the law says that they are to be allowed a 6 percent on their investment, invested capital, if that is what the law says, then, on the face of it, it appears that allowing them 6 percent on their operating expenditures is not in accordance with the law." (R. 51)

* * * * * * *

"The Court: Yes, but I have no method to find out whether the end result is right or wrong, except I based it upon how they [the Commission] went about it. If they included items other than invested capital, why, then, it may be the only conclusion I can draw is that the Commission is allowing more than 6 percent on invested capital. As far as whether it is right or wrong, or whether the company is being properly repaid or not, I do not know anything about that, and I have no means of finding out."[1] (R. 51-52)

* * * * * * *

"The Court: What his argument is, as I understand it, that under the statute, the company should be allowed a rate base which amounts to their invested capital, and if six percent is not enough that the Commission has a perfect right to allow 6½ or 7 or 10 or anything else, but that that is the way they should do it, and not allow as part of the rate base operating expenses; one reason being that you are creating a

[1] The record of the proceedings certified to the Court pursuant to statutory requirement (Section 43-705 of the Code) furnishes the means of determining such questions.

terrible precedent. The first thing you know, some commission will simply say, Well, all the company's operating expenses will be allowed them as a rate base, and they can keep all the profits. It is just a bad way for a judicial tribunal to handle the situation. It is a precendent that it seems to me at the minute is a bad precedent." (R. 61)

Both the District Court and the respondent show that it was the method used in determining the rate base that, in their view of the law, made the Commission's order invalid, as shown by the following colloquy:

"The Court: What is your view of the allowance of this $1,744,000 and this $2,797,000 as a precedent? In other words, expressed in another way, is it your view that if the Public Service Commission felt that the company was not getting a proper return, it should have increased the 6 percent to some other percent rather than apparently evading the real issue by making these allowances?

"Mr. Baker: Your Honor has stated my position better than I could do so myself." (R. 61)

Decision of the Court of Appeals

The Court of Appeals agreed with the District Court "that the Commission's order should be vacated and set aside, but our reasons differ materially, as will appear from the detailed discussion below" (R. 1043).

The Court of Appeals did not decide a single issue raised by the petition of appeal. It did not agree with a single issue decided by the District Court. It did not find error in a single conclusion reached by the Commission. It made no determination whether the rate order is unjust and unreasonable in its consequences.

Under the subject of *Rate of Return* the Court of Appeals held that the traditional formula for rate making "required a determination of the rate base and of a rate of return

on that rate base'' sufficient to produce adequate revenues above operating revenue deductions to pay interest, dividends, and, in general, to maintain the financial integrity of the enterprise. The Court of Appeals said the Commission made no inquiry whatsoever into issues necessary to the determination of a fair rate of return, and said it was this sort of inquiry that this Court referred to at page 605 of its decision in *Colorado Interstate Gas Co.* v. *F. P. C.*, 324 U. S. 581.[2]

The Court of Appeals said:

> ''Failure to subject this issue to inquiry at the hearing and the consequent inadequacy of the record and the findings render the Commission's conclusion that the rates are 'reasonable, just, and non-discriminatory' devoid of substance and wholly ineffective for its purpose'' (R. 1045).

The Court said that without evidence ''at the hearing'' on this essential issue ''there is no basis for application of any standard and the judicial review authorized by the statute becomes a formal but futile gesture''[3] (R. 1045).

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[2] The language quoted by the lower Court from the *Colorado Interstate* case deals solely with the question of original cost of Production and Gathering Facilities. It does not refer to a rate of return.

[3] In 1945 the Commission made a complete study of the Company's cost of capital, and found upon that basis that a rate of return of 6% would be a fair rate of return to be allowed the Company. In addition to the cost of servicing debt and dividends on the stock, the Commission's witness presented a study of earnings price ratios and dividend price ratios of the common stock of the Company and of the common stock of six operating gas utilities, including the Company. The witness testified that in his opinion the rate of return prescribed by the Commission should remain in effect until further order of the Commission "so that it would not again be necessary to review this question in the immediate future unless changed conditions indicated that such a review is warranted." The Commission adopted this recommendation and established a rate of return of 6% "until further order of the Commission." The Findings and Opinion show that the rate of return established does not include an element for the risk of abandonment of property. Findings, Opinion and Order No. 2944, 61 P.U.R. (N.S.) 40 (R. 773-778). The $750,000

The Court of Appeals erroneously stated in its opinion and in its Footnote 24 that the most recent proceeding of the Commission involving the determination of a rate of return to be allowed to the Company was in 1943 by its Order No. 2682. Order No. 2682 was vacated by the District Court because "there was no substantial evidence before the Commission" to support its finding that 5¾% was a fair rate of return. *Washington Gas Light Co.* v. *Public Utilities Commission,* 55 F. Supp. 627. The Commission then made another investigation in 1944, as shown by its Findings and Opinion and Order No. 2827, 56 P. U. R. (N. S.) 238 (R. 767-773). In 1945 it again investigated the rate of return to be allowed to the Company on the basis of cost of capital, and by its Findings and Opinion and Order No. 2944, 61 P. U. R. (N. S.) 40 (R. 773-778) established the rate of 6% to be allowed "until further order of the Commission".

In respect of abandoned property, the Court of Appeals held that it is relevant "to determine whether or not investors have, during the useful life of this property, been compensated for assuming the risk that it would become inadequate or obsolete before the investment in it was entirely recovered".[4] The Court stated that the Commission must first make an inquiry into whether or not the risk of obsolescence in the sense used by the Court "was borne by the investor in the past and whether he was compensated for it".[5]

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rate increase granted was designed to produce revenues that would produce a rate of return of less than 5¾% on the rate base found by the Commission.

[4] The witnesses for the Commission, the Government, and the Company testified that the amount included by the Commission for abandoned property was the net unrecovered investment (R. 181, 182, 193, 197, 198, 207, 212, 497, 585, 611). There was no testimony to the contrary.

[5] Order No. 1458, 11 P.U.R. 469 (R. 737-750), promulgated in 1935, established a basic rate of return of 6½% to be allowed to the Company. There is no indication in the order that the rate of return included an

The Court of Appeals remanded the proceeding to the Commission. It said: "So far as the future is concerned, elimination of the risk of obsolescence will require that the rate of return allowed the Company be lower than one which compensates for" the risk that a particular plant would became obsolete. The Court said that while it thought the *Hope* doctrine precluded it from forbidding the Commission "to include abandoned property in the rate base, we are convinced that protection of the consumer interest requires that such treatment of abandoned property be offset in the rate of return" (R. 1050).

Under the subject of "*Depreciation*" the Court of Appeals said:

> "Even if the Commission ultimately concludes that the unrecovered value of the abandoned property may be included in the rate base, there is some question as to what that amount should be. Appellee challenged the Commission's deduction from the value of the abandoned plant of an allocable portion of the book

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element for the risk of obsolescence. In 1938 the Commission investigated the matter of the rate of return to be allowed the Company, and after such investigation it did not change the rate established in 1935. No consideration was given in this investigation to an element or risk for obsolescence. Order No. 1711, 25 P.U.R. (N.S.) 332 (R. 755-759). In 1943 the Commission by its Findings and Opinion and Order No. 2682 made a study of the rate of return predicated upon the cost of capital and established a rate of 5¾%, which order was vacated by the District Court for lack of supporting evidence. In 1944 the Commission again investigated the question of the rate of return to be allowed the Company. The study was based solely upon the cost of capital and did not include an element for the risk of obsolescence. Based upon the cost of capital, the Commission reduced the rate of return from 6½% to 6%. Findings and Opinion and Order No. 2827, 56 P.U.R. (N.S.) 238 (R. 767-773). In 1945 the Commission again investigated the question of the rate of return to be allowed to the Company on the basis of the cost of capital, and determined that 6% was a fair rate to be allowed "until further order of the Commission." The Findings and Opinion show that the rate of return established did not include an element for the risk of obsolescence. Findings and Opinion and Order No. 2944, 61 P.U.R. (N.S.) 40 (R. 773-778).

reserve for depreciation rather than of the larger actual depreciation as measured by the straight-line method and represented by the reserve requirement''[6] (R. 1050).

The Court stated that the Commission based its action upon the conclusion that the annual charges to depreciation during most of the life of the property were too low and that deduction of the amount of the abandoned property would leave the reserve dangerously low. It said "the record contains no evidence as to whether earnings during the life of this property sufficiently exceeded the fair rate of return to compensate investors for the inadequate depreciation charges".

The Court of Appeals stated that it did not disturb the Commission's classification of the East Station as a standby plant, but added that the same inquiry must be made in reference to it as to abandoned property.[7] It held that the Commission must determine whether or not during the life of the property earnings had exceeded a fair rate of return to compensate investors for the inadequacy of

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[6] The respondent (appellee below) did not raise in his petition of appeal a question as to the amount of the unrecovered investment in abandoned property or as to the amount of the allocable portion of the book reserve for depreciation. He did not raise the question as to whether book reserve or a reserve requirement should be used (R. 1-5). He did not raise any of these questions in his application for reconsideration (R. 135-145), which is a statutory prerequisite to arguing such questions on appeal (Section 43-704 of the Code). Furthermore, the Findings, Opinion and Order No. 3487, 78 P.U.R. (N.S.) 82 (R. 713-726), show that the Commission rejected the reserve requirement study, made in 1947, as "excessive," and said, "it is not now necessary to make a definite finding or even express an opinion upon the total extent to which the computed reserve requirement appears to be excessive."

[7] The respondent's petition of appeal (R. 1-5) and his application for reconsideration (R. 135-145) did not raise the question that the unrecovered cost of the standby plant at East Station was improperly included in the rate base. The unrecovered cost was not in dispute. The witnesses for the Commission, the Government, and the Company included the same amounts for the standby plant in their separate determinations of a proper rate base.

past depreciation charges. The Commission's Order No. 3261 (R. 727-730) shows that the change-over from mixed to natural gas "clearly produced or will produce a loss in the service value of the property in question that could not have been foreseen and provided for." Accordingly, the Commission authorized the unrecovered cost at that time of a little more than five million dollars to be depreciated on an accelerated basis for ten years from January 1, 1948.[8]

In respect of depreciation of the East Station, the Court of Appeals said that what it had said in this regard in connection with the West Station applies here, and that there still remains the determination of whether or not investors "have already been compensated for the risk that annual depreciation charges would prove inadequate at the time of retirement, because of obsolescence."[9]

The Court affirmed the judgment of the District Court on the grounds stated in its opinion. It said:

> "We hold that the Commission's order is invalid because of the inadequacy of the record and findings with regard to rate of return, abandoned property and the standby plant. We do not disturb the Commission's treatment of conversion costs, but with respect to that and to rate base, we have raised considerations which should be weighed in any further proceedings" (R. 1053).

The considerations raised by the Court of Appeals which it said "should be weighed in any further proceedings" were not raised in the application for reconsideration of the rate order nor in the petition of appeal.

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[8] The Federal Power Commission by order dated October 21, 1947, 71 P.U.R. (N.S.) 159, authorized the Company to amortize the abandoned property and to accelerate the depreciation on the standby plant at East Station on a ten-year basis from January 1, 1948. It found the unrecovered cost of the standby plant was the same amount found by this Commission at that time.

[9] See footnotes 3 and 8.

Proceedings Before the Commission

After statutory notice, public hearings were held by the Commission on the Company's application on July 28, August 30 and 31, September 19, 20, 21, 22, 23, 26, 27, and 29, and October 10 and 11, 1949.

The Company's testimony showed that for the calendar year 1948 it earned a return of 4.25% on its average investment during the year, and for the test period of twelve months ended May 31, 1949, a rate of 3.38% (R. 81, 82). Testimony presented by the Commission's witness showed that during the test period the Company earned 3.70% on the weighted rate base for that period (R. 83).

The difference in the rate of return established by the Company's witness and the Commission's witness for the test period was due to a difference in the rate base used by each and a slight difference in the method used by the two witnesses in allocating property not used in the District. The Company's witness included in his rate base an amount representing the appraised value of land in 1932, instead of the original cost of such land. The Commission's witness included land at its original cost.

The witness for the Government excluded from his rate base the unrecovered cost of abandoned property and the unrecovered cost of adapting customers' appliances, and he amortized these amounts as operating revenue deductions on a fifteen-year basis instead of ten years (R. 85-86, 609-610). Upon the rate base so established, and by amortizing on a fifteen-year basis instead of ten, the Government's witness arrived at a rate of return of 4.89% for the test year (R. 85).

No other witness testified on the subject of the elements of the rate base. There was no dispute as to the amount of the unrecovered cost of the abandoned property allocable

to the District of Columbia and the unrecovered cost of the conversion of customers' appliances.

The Commission's witness testified that the unrecovered cost of abandoned plant allocable to the District of Columbia represents the net investment or the depreciated cost of such property which had not been recovered (R. 147, 193, 197, 198). He testified that that part of investment in abandoned property which had not been recovered was because the depreciation reserve which had been established in accordance with the directions of the Commission was not adequate to provide for the loss when it was sustained (R. 206, 497, 498), and that the past provisions for depreciation were inadequate (R. 208, 495).

The Company's witness also testified that the unrecovered cost in abandoned property was the net extraordinary property loss for the test period (R. 181, 182, 212).

The Commission's Findings and Opinion accompanying Order No. 3600 discussed the testimony of the various witnesses in respect of the various issues and the differences among the witnesses where there is a difference of view in respect thereof, and then stated its conclusions in respect of each matter (R. 80-100). The Commission then discussed the effect of the rate increases proposed by the Company (R. 100-101) and the proposed rate schedules (R. 101-102) and its general conclusions from the testimony of record (R. 102-105).

The Commission found that the prudent investment rate base for the test year ended May 31, 1949, amounted to $32,240,198.76, which included the unrecovered cost of abandoned property and the unrecovered cost of converting cus-

[10] It follows from the provisions of Order No. 3261 (R. 729-730) that all of the amounts representing the property already abandoned, the standby plant at East Station to be abandoned, and the conversion costs, will have been written out of the rate base ten years from January 1, 1948.

tomers' appliances. It found that on the basis of the income for the period developed by the Commission's witness the Company earned a return of 3.7% on that rate base. It said that "a return of less than 4% is obviously inadequate to maintain the Company in a sound financial position" (R. 102-103).

The Commission denied the Company's request for an increase of $900,000 in the aggregate on an annual basis and found that rate schedules calculated to produce an increase of $750,000 when applied to the volume of gas sold in the District of Columbia during the calendar year 1948 would provide the Company "with a reasonable return in the immediate future and, at the same time, will confine the burden on consumers to the minimum necessary under the circumstances" (R. 104). The increase granted will produce a rate of return of less than 5¾% on the rate base established by the Commission. From the testimony and the Commission's findings thereon, it concluded "that the rates specified in the order attached to this opinion are just, reasonable and non-discriminatory and will permit the Company to earn a fair return upon its investment devoted to public service and to maintain its financial integrity" (R. 105).

Specification of Errors to Be Urged

The United States Court of Appeals for the District of Columbia Circuit erred:

1. In affirming the judgment of the District Court.
2. In vacating the Commission's rate order without considering or deciding whether the total effect of the order is unjust and unreasonable.
3. In holding that the Commission's order is invalid because of the inadequacy of its findings.
4. In holding the Commission's order invalid upon issues

not raised in the petition of appeal, when the complainant admitted "that the facts are as stated by the Commission in its report".

5. In vacating the Commission's order because the prudent investment rate base included the undisputed unrecovered cost of abandoned property, on the suspicion that during the life of the property the rate of return allowed the Company might have included an element for the risk of abandonment.

6. In vacating the order prescribing rates to produce a rate of return of less than 5¾% because the Commission did not "at the hearing" in the instant proceeding make a new investigation of the rate of return to be allowed.

7. In holding that the traditional formula for rate making requires a determination of a rate base "and of a rate of return on that rate base" in every proceeding in which rates are prescribed.

8. In holding that the "most recent" proceeding by the Commission in the determination of a fair rate of return was in 1943.

9. In vacating the rate order designed to produce a rate of return of less than 5¾% because "There is nothing before us to indicate that pertinent local conditions and economic conditions generally have remained static during the intervening years" since the Commission last made an investigation and determined that 6% was a fair rate of return predicated on the cost of capital.

10. In vacating the Commission's order prescribing rates to produce a rate of return of less than 5¾% on the ground, "Nor does it appear that the risk factor, so important an element in fixing rate of return, has remained static" since the Commission, on the basis of cost of capital, determined that 6% was a fair rate of return to be allowed the Company.

11. In vacating the order and remanding the proceeding to the Commission with instructions that if the prudent investment rate base includes the unrecovered cost of abandoned property "that such treatment of abandoned property be offset in the rate of return".

12. In vacating the Commission's order and remanding it to the Commission with instructions that, if the prudent investment rate base includes the unrecovered cost of abandoned property, the Commission also investigate and determine whether, during the life of the said property, the rate of return included an element for the risk of abandonment.

13. In vacating the Commission's order because "the record contains no evidence as to whether earnings during the life of this property sufficiently exceeded the fair rate of return to compensate investors for the inadequate depreciation charges".

14. In vacating the Commission's order because it failed to determine "whether or not investors have already been compensated for the risk that annual depreciation charges would prove inadequate at the time of retirement, because of obsolescence".

15. In holding that the rate of return to be allowed must "be offset" by an element for the risk of abandonment of property.

16. In holding that the respondent "challenged the Commission's deduction from the value of the abandoned plant of an allocable portion of the book reserve for depreciation rather than of the larger actual depreciation as measured by the straight-line method and represented by the reserve requirement".

17. In vacating the Commission's rate order on the suspicion that a different kind of investigation might have produced different results, without considering or de-

ciding whether the total effect of the rate order is unjust and unreasonable.

Reasons for Granting the Writ

The Court of Appeals has decided a matter of great national interest in the regulatory process and in rate making that touches upon and will affect the administrative practice and administrative determinations of Federal and state regulatory bodies relating to the fundamental elements of rate making. It is the belief of the petitioner that this is the only decision of its kind in any Circuit Court of Appeals.

The decision of the Court of Appeals is contrary to and in conflict with fundamental rate-making principles enunciated by this Court and followed by the other Circuit Courts of Appeals. It is contrary to the decisions of this Court and other Circuit Courts of Appeals that have been followed by Federal and state rate-regulatory agencies for many years.

1. The decision of the Court of Appeals is directly contrary to what this Court said about judicial reviews in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591; *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575; *Rochester Telephone Corp.* v. *United States*, 307 U. S. 125; *St. Joseph Stock Yards Co.* v. *United States*, 298 U. S. 38; *Mississippi Valley Barge Line Co.* v. *United States*, 292 U. S. 282; and other cases.

The decision is contrary to what this Court said in the *Hope* case at p. 602 that "If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end", and what this Court said in the *Natural Gas Pipeline* case at p. 586 that if the rate order as applied to the facts "and viewed in its entirety, produces no arbitrary result, our inquiry is at an

end", and what this Court said in the *Mississippi Valley Barge Line* case at p. 287 and in the *Rochester Telephone* case at p. 146 that "The judicial function is exhausted when there is found to be a rational basis for the conclusions approved by the administrative body".

The judicial inquiry by the Court of Appeals went beyond the limits defined by this Court in the *St. Joseph Stock Yards* case, *supra*, that "judicial inquiry into the facts goes no further than to ascertain whether there is evidence to support the findings" (p. 51). The Court of Appeals "raised considerations" outside of the record which it said "should be weighed in any further proceedings". Upon such other considerations the Court of Appeals vacated the Commission's order and remanded it, even though this Court said in the *Stock Yards* case that findings by a legislative agency "will not be disturbed save as in particular instances they are plainly shown to be overborne" (p. 54).

In its review, the Court of Appeals started where this Court said in the *Hope* case judicial inquiry "is at an end". It completely passed over and ignored the keystone of the doctrine of the *Hope* case. It neither considered nor determined whether "the total effect of the rate order" under review was unjust and unreasonable.

The Court of Appeals started its judicial inquiry by raising a number of suspicions that were not raised by the respondent in his application for reconsideration of the rate order nor in his petition of appeal. The Court started its judicial inquiry with the suspicion that during the life of the property represented in the rate base earnings might have "sufficiently exceeded the fair rate of return to compensate investors for the inadequate depreciation charges" (R. 1050), and because of this suspicion the Commission might have determined an erroneous rate base by deducting from the original cost of property the book reserve

for depreciation rather than a reserve requirement—a question not raised by the respondent.

Without considering or determining the total consequences of the rate order, the Court of Appeals further pursued its judicial inquiry by asserting, contrary to fact, that the respondent challenged the deduction of book reserve instead of a reserve requirement from the original cost of property (R. 1050) and raises the suspicion that for that reason the rate base may be too high. The suggestion that "the larger actual depreciation" as measured by the reserve requirement should be deducted from original cost in determining the rate base is in the face of the Commission's rejection in 1947 of a reserve requirement study as "excessive" when the Commission said "it is not now necessary to make a definite finding or even express an opinion upon the total extent to which the computed reserve requirement appears to be excessive" (R. 720).

Furthermore, the respondent's application for reconsideration of the rate order (R. 135-145), which is prerequisite to an appeal (Section 43-704 of the District Code) and the petition of appeal (R. 1-5) show that the deduction of the book reserve from original cost was not challenged and that no claim was made that the reserve requirement study made in 1947 should be used in 1949. To the contrary, the respondent admitted "that the facts are as stated by the Commission in its report" (R. 23) and that he does "not question any of the basic findings of fact of the Commission" (R. 57). The petition of appeal shows that only the conclusions of the Commission were challenged, and challenged "as a matter of law."

The Court of Appeals pursued its judicial inquiry further by raising another suspicion not raised by the respondent, that during the useful life of abandoned property and that to be abandoned because of conversion to the sale of straight natural gas the investors might have "been com-

pensated for assuming the risk that it would become inadequate or obsolete before the investment in it was entirely recovered" (R. 1048-1049). This suspicion is contrary to undisputed evidence in the record that the amount included for this property is the net investment or the depreciated original cost which had not been recovered (R. 181, 187, 193, 197, 198, 207) and that the depreciation accruals allowed by the Commission had been inadequate "to provide for loss when it is sustained" (R. 306, 497, 498). It is contrary to the Commission's finding that a substantial amount of the unrecovered cost of abandoned property was due not only to the change-over to natural gas but to "inadequate depreciation accruals in the past" (R. 722) and that it "could not reasonably have been foreseen and provided for" (R. 729). This suspicion is also contrary to the Commission's finding in the matter of depreciation accruals of the Company in 1949, when it said that rates charged for gas service by the Company have been closely regulated and accruals for depreciation "have constituted an important factor in the determination of such rates" (R. 722).

The Court of Appeals continued its judicial inquiry by raising another suspicion not raised by the respondent, that the rate of return used by the Commission to test the reasonableness of the rates prescribed by it might not be the fair rate of return. That question was not raised by any party before the Commission or the lower Courts. The Commission made a study in a public investigation of the Company's cost of capital, indicated by this Court in the *Hope* case as a proper method of balancing the interests of the investor and consumer. The Commission's witness in that proceeding recommended that a rate of return be established for the future predicated upon the cost of capital so that it would not again be necessary to review the question of the rate of return to be allowed the Company "unless changed conditions indicated that such a review

is warranted" (R. 775). The Commission approved that recommendation and reduced the rate of return from 6½% to 6% "until further order of the Commission" (R. 777). The rate of return allowed by the Commission in the instant proceeding is less than 5¾%.

In remanding the proceeding to the Commission, the Court of Appeals instructed the Commission that "so far as the future is concerned, elimination of the risk of obsolescence will require that the rate of return allowed the Company be lower than one which compensates for such risk" (R. 1050), when the record shows that the rate of return does not include an element for the risk of obsolescence (R. 737-750, 767-771, 773-777).

Vacating the Commission's order because it did not "at the hearing" in the instant proceeding make a new determination and finding of a rate of return is directly in conflict with this Court's holding in *Vinson* v. *Washington Gas Light Co.*, 321 U. S. 489. The instant proceeding is a parallel to the proceeding in that case. There the Commission used the rate of return of 6½% which had been determined by the Commission seven years earlier as the fair rate of return. In the instant proceeding the Commission prescribed rates to produce a rate of return of less than 5¾%.

Without considering or deciding whether the total effect of the Commission's order was unjust or unreasonable, the Court of Appeals vacated it upon these suspicions not raised by the respondent and not argued in the Courts below. These suspicions were used to overcome the presumption of validity attaching to administrative findings; and to upset "the entire legislative process, embracing the method used in reaching the legislative determination as well as that determination itself."* By vacating the Commission's order upon these suspicions the Court lifted the burden from the shoulder of the respondent of making a convincing

*Los Angeles Gas & Electric Corp. v. Railroad Com., 289 U.S. 287, p. 304.

showing that the order, when "viewed in its entirety," is unjust and unreasonable in its consequences.

2. The Court of Appeals did not affirm the judgment of the District Court on a single issue decided by that Court. It did not decide a single issue raised by the petition of appeal. It did not vacate the Commission's order on a single conclusion reached by the Commission.

The Commission's findings are predicated upon the evidence of record before it. The property included in the plant accounts was not in dispute. The amount of the unrecovered cost in abandoned property and the amount of the unrecovered cost of adapting customers' appliances were not in dispute. The amount of the book reserve which was deducted from the original cost of property was not in dispute. While there was some dispute as to certain items included in the operating expenses, the Commission discussed the testimony of the various witnesses on the subject and stated its conclusions thereon.

Clearly, there was a rational basis for the conclusions reached by the Commission. In the *Rochester Telephone* case, *supra*, this Court said that, having found that the record permitted the rate making body to draw the conclusions that it did, "a court travels beyond its province to express concurrence therewith as an original question" (p. 146). This Court has many times held that administrative action is not arbitrary if any set of facts reasonably can be conceived which would sustain the action. This Court has also said that even if the validity of action taken by an administrative body is fairly debatable, the administrative judgment must be allowed to control. *Radice* v. *New York*, 264 U. S. 292; *New York Rapid Transit Corp.* v. *City of New York*, 303 U. S. 573. The courts do not sit as boards of revision of administrative determinations. *Los Angeles Gas & Electric Corp.* v. *Railroad Commission*, 289 U. S. 287.

3. The action of the Court in vacating the Commission's order because of the inadequacy of its findings is contrary to decisions of this Court. *Alabama Great Southern Railroad Co.* v. *United States,* No. 45, October Term, 1950, decided January 2, 1951, Vol. 95, No. 5, p. 190, Advance Opinions; *United States* v. *Pierce Auto Freight Lines, Inc.,* 327 U. S. 515, 529; *Manufacturers R. Co.* v. *United States,* 246 U. S. 457, 487, 489-490.

4. Contrary to decisions of this Court, the Court of Appeals vacated and remanded the Commission's order with instructions to substitute the Court's judgment as to (1) the method of measuring a component of the rate base, (2) the deduction of a depreciation reserve requirement from the original cost of property in establishing the rate base instead of the book reserve for depreciation, (3) the method of determining the rate of return to be allowed in this proceeding and "So far as the future is concerned", and (4) the kind of investigation to be conducted. It said:

> "Although we think the *Hope* doctrine precludes us from forbidding the Commission to include abandoned property in the rate base, we are convinced that protection of the consumer interest requires that such treatment of abandoned property be offset in the rate of return." (R. 1050.)

The Court remanded the proceedings to the Commission and stated in its opinion that:

> "Failure to subject this issue [the rate of return] to inquiry at the hearing and the consequent inadequacy of the record and the findings render the Commission's conclusion that the rates are 'reasonable, just, and nondiscriminatory' devoid of substance and wholly ineffective for its purpose" (R. 1045).

The Court said that "Even if the Commission ultimately concludes that the unrecovered value of the abandoned

property may be included in the rate base, there is some question as to what that amount should be" (R. 1050). The Court then proceeded to state that the appellee (respondent) challenged the Commission's deduction of the book reserve for depreciation from the original cost rather than "the larger actual depreciation" as represented by the reserve requirement (R. 1050). The respondent did not raise this question in his petition of appeal.

The Court went beyond its power of judicial review in indicating that a reserve requirement should be deducted from the original cost in determining the rate base, rather than the book reserve (R. 1050).

The Court of Appeals held the Commission's order invalid, but did not disturb the Commission's treatment of conversion costs. However, it added, "but with respect to that and to rate base, we have raised considerations which should be weighed in any further proceedings" (R. 1053). Thus the Court, by remanding the proceedings to the Commission, has instructed it as to the kind of investigation it shall conduct; the method by which it shall determine an element of the rate base; the method by which it shall determine the rate of return to be allowed; and the method by which original cost shall be reduced, by a reserve requirement study rather than by the book reserve for depreciation.

These instructions are contrary to and in conflict with the often declared statement that courts do not sit as boards of revision of administrative orders.

The considerations raised by the Court of Appeals which it said "should be weighed in any further proceedings" are instructions to the Commission which are contrary to the decisions of this Court: in *Interstate Commerce Commission* v. *Inland Waterways Corp.*, 319 U. S. 671, 691, where the Court said, "Nor are we at liberty to prescribe general attitudes the Commission must adopt towards the

exercise of discretion left to it rather than to courts. We decide only whether the Commission has acted within the power delegated to it by law"; and what this Court said in the *Hope* case at pp. 617-618 that "Apart from the requirements of judicial review it is not for us to advise the Commission how to discharge its functions"; and what this Court said in *United States* v. *Los Angeles & S. L. R. Co.*, 273 U. S. 299, 311, that "Congress did not confer upon the courts power, either to direct what this 'tribunal appointed by law and informed by experience' (citation) shall find or to annul the report, because of errors committed in making it".

Conclusion

For the reasons stated, it is respectfully submitted that this petition for a writ of certiorari should be granted.

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February, 1951.

APPENDIX

D. C. Code, § 43-301 (37 Stat. 977)

That every public utility doing business within the District of Columbia is required to furnish service and facilities reasonably safe and adequate and in all respects just and reasonable. The charge made by any such public utility for any facility or services furnished, or rendered, or to be furnished or rendered, shall be reasonable, just, and nondiscriminatory. Every unjust or unreasonable or discriminatory charge for such facility or service is prohibited and is hereby declared unlawful. Every public utility is hereby required to obey the lawful orders of the commission created by this section.

D. C. Code, § 43-704 (49 Stat. 882)

* * * That any public utility or any other person or corporation affected by any final order or decision of the commission may, within thirty days after the publication thereof, file with the commission an application in writnig requesting a reconsideration of the matters involved, and stating specifically the errors claimed as grounds for such reconsideration. No public utility, or other person or corporation shall in any court urge or rely on any ground not so set forth in said application. The commission, within thirty days after the filing of such application, shall either grant or deny it. Failure by the commission to act upon such application within such period shall be deemed a denial thereof. If such application be granted, the commission, after giving notice thereof to all interested parties, shall, either with or without hearing, rescind, modify, or affirm its order or decision. The filing of such an application shall act as a stay upon the execution of the order or decision of the commission until the final action of the commission upon the application: *Provided,* That upon written consent of the utility such order or decision shall not be stayed unless otherwise ordered by the commission. No appeal shall lie

from any order of the commission unless an application for reconsideration shall have been first made and determined.

D. C. Code, § 43-706 (49 Stat. 883)

In the determination of any appeal from an order or decision of the commission the review by the court shall be limited to questions of law, including constitutional questions; and the findings of fact by the commission shall be conclusive unless it shall appear that such findings of the commission are unreasonable, arbitrary or capricious.

Nos. 540 and 548

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1950

No. 540

WASHINGTON GAS LIGHT COMPANY, *Petitioner*,

v.

VERNON V. BAKER, *Respondent*.

No. 548

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA, *Petitioner*,

v.

VERNON V. BAKER, *Respondent*.

On Petitions for Writs of Certiorari to the United States Court of Appeals for the District of Columbia Circuit.

BRIEF FOR VERNON V. BAKER IN OPPOSITION.

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Natural Gas Act (52 Stat. at L. 821, 15 U.S.C. 717).. 12

IN THE

Supreme Court of the United States

OCTOBER TERM, 1950

No. 540

WASHINGTON GAS LIGHT COMPANY, *Petitioner,*

v.

VERNON V. BAKER, *Respondent.*

No. 548

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA, *Petitioner,*

v.

VERNON V. BAKER, *Respondent.*

On Petitions for Writs of Certiorari to the United States Court of Appeals for the District of Columbia Circuit.

BRIEF FOR VERNON V. BAKER IN OPPOSITION.

OPINIONS BELOW.

The Opinion of the United States Court of Appeals for the District of Columbia Circuit (not yet officially reported) appears at R. 1041-1053. The Opinion of the District Court (not reported) appears at R. 10-18. The Opinion and Order of the Public Utilities Commission of the District of Columbia, dated November 9, 1949, appears at R. 77-117 (83 PUR NS 4).

JURISDICTION.

The judgment of the Court of Appeals was entered on December 21, 1950 (R. 1054). The jurisdiction of this Court is invoked under 28 U. S. C. 1254, and Section 43-705 of the District of Columbia Code (1940). (Act of March 4, 1913, 37 Stat. 989, Ch. 150, § 8, par. 65; amended, August 27, 1935, 49 Stat. 882, Ch. 742, § 2.)

QUESTIONS PRESENTED.

The basic issue is whether the Court of Appeals exceeded a proper scope of review in the grounds it assigned for affirming the Order of the District Court (R. 19), which vacated and set aside the Order of the Commission and remanded the case for further proceeding. Petitioner's designation of questions are confusing and do not clearly set forth the basic issues. Respondent sets forth the following as a clearer statement of the questions presented:

1. Does the scope of review delineated in the *Hope* case prohibit a Court of Appeals from invalidating an order of an administrative agency on the grounds of absence of necessary findings and lack of substantial evidence?

2. Did the Court of Appeals in invalidating the order of the Commission on the grounds of inadequacy of the record and findings with regard to the rate of return, abandoned property and the standby plant substitute its judgment for that of the Commission in the selection of a formula for the determination of the reasonableness of rates?

3. Was the Court of Appeals precluded from invalidating the order of the Commission on the grounds of absence of findings and inadequacy of record with respect to rate of return when the Commission made no record or finding on such issue?

STATUTES INVOLVED.

The pertinent provisions of the District of Columbia Code (1940) are set forth in the Appendix.

STATEMENT.

The Opinion Below.

The Court of Appeals held that the Commission's order granting a rate increase was invalid "because of the inadequacy of the record and findings with regard to the rate of return, abandoned property and the standby plant." (R. 1053.) In its Opinion, the Court below observed that the Commission "made no inquiry whatsoever into issues necessary to determination of a fair rate of return." (R. 1044.) The Opinion, referring to *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 88 L. Ed. 333, specifically cited the absence of any evidence on or consideration of the costs of capital and comparisons with the return on investments in other enterprises having a similar risk factor. The Court concluded that (R. 1045):

> "Failure to subject this issue to inquiry at the hearing and the consequent inadequacy of the record and the findings render the Commission's conclusion that the rates are 'reasonable, just and non-discriminatory' devoid of substance and wholly ineffective for its purpose."

In its discussion of the abandoned and removed property (West Plant) and the unused standby plant (East Plant), which were included by the Commission in the rate base in an amount stated to represent the unrecovered cost of such properties, the Court of Appeals, unlike the District Court, held that the provision of Section 43-306 of the District Code did not require the exclusion of such property on the ground that it was not "used and useful in the public service." In view of this statutory interpretation, the Court concluded that the composition of the rate base was within the province

of the Commission under the doctrine of the *Hope* case. The Court held, however, that the principles of that case required that, if such property is to be included in the rate base, it must be done on a basis which protects both the interests of the investor and the consumer. Bearing on this problem, the Court stated was the question whether the investors have in the past been compensated for assuming the risk that the property would become inadequate or obsolete before the investment in it was entirely recovered. The Court did not presume to make a determination of this fact and stated that such an inquiry must be made in the first instance by the Commission. The Court's criticism was directed to the fact that, although the Commission's conclusion depends upon the premise that inadequate charges for depreciation were made in the past which resulted in lower revenues to investors than they would otherwise have received, the record contains no evidence upon which the soundness of this premise could be tested. (R. 1050)

The Court below also raised questions about the Commission's determination of the rate base and the treatment of conversion costs. Since the case was decided on the grounds discussed above, the Court stated there was no need to discuss the question of whether there was sufficient evidentiary support for the Commission's treatment of these items. The Court pointed out, however, that there was lack of clarity in the record as to the method used by the Commission in arriving at the rate base. The Court noted the failure of the Commission to refer in its Findings and Opinion to the basic valuation order (R. 796-912), and to the absence of a computation of net additions since the date of such order. With respect to conversion costs, the Court took the view that under the *Hope* case, it is for the Commission to determine whether such costs are includible in a rate base, even though not reflected in tangible property additions to the company's plant. The Court also pointed out that conversion resulted in benefits to the investor as well as to the consumer, and that, therefore, the propriety of the inclusion of such costs

in a rate base should be determined in the light of a balancing of the investor and consumer interests. (R. 1052)

The Petitioners have sought to cast the Opinion of the Court below in a different mold. The Petitioners contend that the Opinion of the Court below transcends the bounds of judicial review permitted under the doctrine of the *Hope* case, and that the Court below has invaded the realm of the administrative function and has substituted its judgment for that of the Commission in requiring that a determination should be made with respect to a fair rate of return, and with respect to the factors affecting the balance between the investor and consumer interests on such matters as the inclusion of property wholly or partially obsolete. The Petitioners further contend that these issues, particularly that relating to a determination of the fair rate of return, was not properly presented to the Court and that, accordingly, the Court could not appropriately take such issues into consideration.

Proceedings Before the Commission.

The Respondent as an individual rate payer did not enter an appearance in the proceedings before the Commission and was not a party thereto, although the Federation of Citizens Associations of the District of Columbia, with whom he is affiliated as Chairman of its Public Utilities Commission did enter an appearance, and an extensive presentation was made before the Commission on behalf of consumer interests. The Federation is a corporation organized under the laws of the District of Columbia and its members are various civic organizations in the community, whose members in turn are residents of the District of Columbia and members of the gas consuming public. The Respondent and the Federation jointly filed a petition for reconsideration (R. 135-145). The Appellee and the Federation took a joint appeal from the order to the Commission (R. 15), but the Federation was dropped as a party as not showing the

proper statutory interest to maintain the action. The Respondent appeared *pro se* before the District Court and successfully argued his own case. Upon the appeal by Petitioners herein from the order of the District Court vacating and setting aside the order of the Commission, the Respondent enlisted the aid of the counsel who are on this brief.

The order of the Commission found a rate base of approximately $32,240,000.00, which includes an amount of approximately $1,744,665.00, representing so called unrecovered cost of abandoned property (West Plant) allocable to the operation of the gas company in the District of Columbia and an amount of approximately $2,700,000.00, representing the unamortized portion of expenditures made by the company in converting customers' appliances for the use of natural gas (R. 88-89; Ex. 19 at R. 603). The Commission authorized the amortization of these items over a period of ten years by annual charges to income (R. 98-99). The Commission also accelerated depreciation of East Plant over the same period of time (R. 98, 727-730). These charges to income aggregate approximately $1,000,000 per annum, and are responsible in large measure for the gas company's request for increased rates.

1. Revenues.

The application of the gas company to the Public Utilities Commission requested an emergency increase of its operating revenues by $900,000.00 on an annual basis (R. 67-75). This application was unsupported by specific rate schedules, which were introduced toward the close of the proceedings before the Commission. In its Findings and Opinion, the Commission rejected the rate schedule proposed by the Commission on the grounds that the rates proposed would result in the production of revenues in excess of $900,000.00 per annum. In reaching this conclusion the Commission pointed out that the revenues estimated to be obtained from proposed rate schedules were based on therm sales actually

made during the calendar year 1948, and that the application of the proposed rate schedules to therm sales during the test year ended May 31, 1949, adjusted for normal temperature conditions, would undoubtedly produce in excess of $900,000.00 (R. 103). The Commission further pointed out that the proposed rate schedules did not take into account growth and volume of business resulting from the connection of additional customers or to reduction in revenue requirements needed to serve a probably declining rate base, which would follow from the amortization of abandoned property and costs of conversion to natural gas. It is also clear from the record that the proposed rates did not take into account revision of certain accounting procedures relating to allocation of promotional costs between operations in the District of Columbia and outside of the District, and to the allocation of costs between utility operations and the non-utility operations of merchandising and jobbing of appliances, which would result in the reduction of operating expenses (R. 90-98). However, the Commission itself made no findings as to future revenues or expenses and no specific forecast of the effect of the rate schedules approved under future conditions.

The rate schedule actually ordered effective was stated by the Commission to be designed to produce annual revenues of $750,000.00 when applied to the sales of gas in the District of Columbia during the calendar year 1948 (R. 104). However, the Commission made no finding with respect to what revenues the rates would produce during the period the rates would be in operation. While the Commission, in rejecting the rates proposed by the company indicated that rates based on the 1948 consumption of gas would have to be subjected to substantial adjustments to reflect normal temperature conditions, the connection of additional customers, and reduced revenue requirements, the Commission made no attempt to reflect such adjustments. For this reason, it is impossible to determine what revenues the rates would produce and what return such revenues would produce, and

whether such return would be a fair return. No estimate of earnings under the rate schedule is made by the Commission and none can be ascertained from the Findings and Opinion. Without such an estimate of the probable future earnings during the period when the rates would be in effect, the Commission's conclusion that the rates are reasonable is obviously arbitrary. The only thing which safely can be said about the revenue which would be produced by the rate schedules is that such revenue would be in excess of $750,000.00 per annum.

Although the Commission did not require that a full record be developed with respect to probable growth in the business, the record does contain isolated bits of evidence on this point which indicates that the connection of new customers in 1949 and 1950 would substantially increase the company's sales. It was stated by a company witness that 95% of the new homes being built in Washington will use gas for space heating (R. 562). This same witness stated that by October, 1949, there were approximately 2,500 more space heating customers than there were at the end of 1948 (R. 560). The record further indicated that the full potential of space heating customers had not been realized due to an order of the Commission in effect between February 1948, and February 1949, restricting the connections of additional space heating customers (R. 787-788). On the basis of evidence in the record to the effect that each space heating customer would produce approximately $100 to $150 revenue per annum, it is clear that the proposed rates would produce revenue substantially in excess of $750,000.00 (R. 398, 487, 569 and Ex. 16 at R. 594).

2. Rate Base.

The Court of Appeals pointed out that there was also lack of clarity and probable lack of evidentiary support for the Commission's conclusion with respect to the rate base (R. 1053). The Court below stated that an examination of the

record "leaves some doubt as to whether the basic valuation figure, of which the present rate base is said to be a projection, represents original cost, reproduction cost, or some other 'fair value' figure." The Court further referred to the failure of the Commission to specifically refer to the basic valuation order or to make any references to the net additions, subsequent to the date of that order.

These comments by the Court below highlight one of the fatal inadequacies in the record before the Commission. While the Commission purports to have made its rate base determination on the basis of the principles of the prudent investment theory, there is no support in the record for a conclusion that the rate base of approximately $32,240,000 found by the Commission reflects unrecovered dollars actually invested in the business. In the first place, it must be recognized that the origins of the company extend back to 1848, and that because of the antiquity of the company there was no complete record of the original cost of the properties. In its valuation order of March 19, 1935 (R. 796-912), the Commission specifically stated that: (R. 887)

> "After carefully considering the entire record we conclude that the original cost of the property cannot be ascertained on this record."

The fact that the property accounts of the Commission were not stated at original cost was again adverted to in an opinion of ex-Commissioner Hankin, concurring in part and dissenting in part, to a rate proceeding in 1943. (R. 944)

Moreover, the record also shows a second and probably more substantial deviation of the rate base from a reflection of unrecovered dollars actually invested in the business. From 1935 through 1947, the company's rates were regulated by agreement pursuant to a sliding scale arrangement unique to the District of Columbia and an alternative to normal regulation. The sliding scale agreement was terminated by action of the Commission prior to the commencement of this proceeding. (R. 737-750, 782-785) This method

of regulation of rates is based on § 43-317 of the District of Columbia Code. (1940) Under the Public Utilities Commission Order inaugurating the sliding scale system of rate regulation for the gas company the initial rate base as of June 30, 1935 was set at $21,000,000.00. (R. 739) This rate base did not purport to represent unrecovered dollars actually invested in the business and was an agreed rate base limited, in the words of the Commission, "for the purposes of such arrangement only." (R. 739) The sliding scale arrangement was put into effect on December 13, 1935 (R. 727). On March 19, 1935, the Commission issued its Order No. 1341, after a comprehensive valuation investigation (R. 796). In that order the Commission found $15,039,000.00 as a final value for the property of the gas company within the District of Columbia as of June 30, 1932 (R. 908). It is important to keep in mind that this valuation was based on cost of reproduction and all other facts normally considered in connection with the "fair value" theory of valuation (R. 799). Ex-Commissioner Hankin, in his opinion referred to above, pointed out that the sliding scale rate base of $21,000,000.00 not only included no deduction for depreciation, but was higher than reproduction cost new as of 1933, plus net additions up to June 30, 1935, and included as of that date approximately $821,000.00, representing the carrying value of land in excess of its original cost (R. 943-944). Upon abandonment of the sliding scale the rate base thereunder, subject to an adjustment of approximately $700,000.00 representing the excess of book accruals for depreciation over the sliding scale depreciation accruals made during the period the sliding scale arrangement was in effect, was carried forward as the rate base of the company (R. 717, R. 585 (Ex. 11), R. 603 (Ex. 19)).

It is thus clear that for many years past the depreciation reserve has been accrued on the basis of inflated property accounts.

In the light of these relevant facts, which were matters of official record with the Commission, it was incumbent upon

the Commission to make further inquiry in order to justify the premise used in its Findings and Opinion that past rates would have been higher if larger depreciation accruals had been permitted. Such an inquiry would include an examination into the historical earnings of the company to determine if they were in fact excessive.

This is the context in which the Court of Appeals held that the order of the Commission was invalid because of the inadequacies of the record and findings with regard to rate of return, abandoned property and the standby plant. It is apparent from the foregoing that the Commission had no record upon which it could make findings either with respect to the revenues to be generated by the new rates or the risks of the business assumed by the investors for which they should now be compensated. There is a complete absence of record and findings with respect to the historical facts upon which a determination could be made that the cost of the abandoned plant and the standby plant have not been recovered by the investors, or whether, if in fact such costs have not been recovered, the investors enjoyed a rate of return in the past which compensated them for assuming the risk of such loss. Prior to the instant case, which is the first occasion on which the Commission has applied the prudent investment formula to this company, the Commission's theory of rate regulation was identified with the fair value cases. As the Court of Appeals points out, under that theory the rate of return allowed the gas company must of necessity have included compensation for the risk of obsolescence, since, under that theory, it was not normal to include in the rate base property not used and useful in the public service.

Quite apart from the historical factors bearing on the balancing of the investor and consumer interest, the Commission made no inquiry into the return necessary under current conditions to attract capital necessary to the operation and growth of the enterprise. In the absence of an inquiry

into such considerations, it is manifest that no conclusion as to reasonable rates supportable under juridical standards could be made.

ARGUMENT.

In our view, these petitions do not raise any questions requiring further review by this Court.

The Petitioners have specified many errors alleged to have been committed by the Court of Appeals, but these assignments of error are overlapping and do not contain a clear cut statement of the issues involved. It would seem that many of the assigned errors are merely unmeritorious arguments, do not raise justiciable issues and can be summarliy dismissed. In this category is the argument that the decision of the Court of Appeals is of nationwide importance. In support of this argument, the decision of the Court below is represented to have general importance, because the Court of Appeals stated that the governing statutes in the District of Columbia give the Public Utilities Commission the same broad authority as is possessed by the Federal Power Commission under the Natural Gas Act. This is clearly a spurious contention which is worthy of no further comment beyond the statement that all orders of the Federal Power Commission are not of general importance. Petitioners also seek to raise the order of the Court below to national significance by the specious argument that the decisions of the Commission will tend to discourage the wide use of natural gas. In response, it must simply be stated that the only apparent deterrent to a universal use of natural gas is the limitation of the nation's natural gas reserves and the location of interstate transmission facilities. It should be pointed out that the assertion that the principles set forth in the opinion below penalize investors in gas distribution companies to the advantage of consumers, simply raises the question of reasonableness of rates, and does not answer it.

This decision is of importance only in the District of Columbia. It involves no constitutional question; in fact, no Federal question, but only the authority of the local regulatory commission to fix rates under a local statute without consideration of pertinent facts necessary to determine the reasonableness of the rates to consumers.

1. The Scope of Review Delineated in the Hope Case Does Not Prohibit a Court of Appeals from Invalidating an Order of an Administrative Agency on the Grounds of Absence of Necessary Findings and Lack of Substantial Evidence.

The Petitioners contend that the action of the Court below, in vacating the Commission's order on the grounds of inadequacy of findings and records, is contrary of decisions of this Court. The Commission expressly raises this question on Page 25 of its petition, and this contention pervades the entire argument of the Company. This issue squarely raises the question of whether the judicial review permitted under the doctrine of the line of decisions centering around the *Hope* case, precludes the Court of Appeals from inquiring into whether the Commission has made all the necessary findings and whether those findings are supported by substantial evidence. It is clear that no such limitation on the scope of judicial review was affected by the doctrine of the *Hope* case. The thrust of the *Hope* case is that judicial review is limited to a determination of whether the total effect of the rate order meets the statutory requirement of justness and reasonableness.

It requires no extended argument to realize that a reviewing Court cannot perform this function under a scope of review which is so limited as to preclude the Court from determining whether proper findings have been made and whether such findings have the evidentiary support required by the statute. *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U. S. 575, 586; 86 L. Ed. 1037, 1050. In that case, the Court pointed out that under the Natural Gas Act,

the Commission's findings of fact "if supported by substantial evidence, shall be conclusive." As indicated by the opinion below, § 43-706 of the District Code contains a similar standard which provides that:

> "the findings of fact by the Commission shall be conclusive unless it shall appear that such findings of the Commission are unreasonable, arbitrary or capricious."

In *Colorado Interstate Gas Company* v. *Federal Power Commission,* 324 U. S. 581, 595, 89 L. Ed. 1206, 1219, this Court has expressly stated that the judicial review is not intended to become a perfunctory process. In *Colorado-Wyoming Gas Company* v. *Federal Power Commission,* 324 U.S. 626, 634; 89 L. Ed. 1235, 1241, this Court amplified its views with respect to the scope of judicial review. It was there said that:

> "But we must first know what the 'finding' is before we can give it that conclusive weight. We have repeatedly emphasized need for clarity and completeness in the basic or essential findings on which administrative orders rest* * * Their absence can only clog the administrative function and add to the delays in rate-making. We cannot dispense with them for Congress has provided the standards for judicial review under this Act, § 19 (b). The courts cannot perform the function which Congress assigned to them in the absence of adequate findings. Nor are they authorized under §19 (b) to make findings and substitute them for those of the Commission."

Mr. Justice Frankfurter's remarks in the dissenting opinion in *City of Yonkers* v. *United States,* 320 U.S. 685, 694; 88 L. Ed. 400, 406, makes clear that judicial review extends to findings not specifically required by statute. In that opinion it was said:

> "But the Courts have also spoken of the need of findings as the basis of validity of an order of the Interstate Commerce Commission in the absence of a Congressional direction for findings. The requirement of

> findings in such a context is merely part of the need for courts to know what it is that the Commission has really determined in order that they may know what to review. 'We must know what a decision means before the duty becomes ours to say whether it is right or wrong.' See *United States* v. *Chicago M. St. P. & P. R. Co.*, 294 U.S. 499, 509-511, 79 L. Ed. 1023, 1031, 1032, 55 S. Ct. 462."

It is clear from the foregoing that the court below did not exceed its proper scope of review in holding invalid the order of the Commission on the grounds of inadequacy of finding and record. The contention of the Petitioners to the contrary is at odds with the precedents cited above. The weakness of the Petitioner's contention in this regard is that it would reduce the reviewing function to a perfunctory process, contrary to the statute and the decisions.

2. The Court of Appeals in Invalidating the Order of the Commission on the Grounds of Inadequacy of the Record and Findings with Regard to the Rate of Return, Abandoned Property, and the Standby Plant Did Not Substitute Its Judgment for That of the Commission in the Selection of a Formula for the Determination of the Reasonableness of the Rates.

The Court below observed that the Commission made no inquiry whatsoever of the issues necessary to determination of a fair rate of return. The Court particularly noted the absence of any record or finding with respect to the costs of capital and the absence of any comparative data with respect to returns on investments in other enterprizes similarly situated. With respect to abandoned property and the standby plant, the Court below did not object to the inclusion of such items in the rate base. Following the *Hope* case, the Court held that inclusion of these items in the rate base, however, must meet the test of justness and reasonableness to the consumer as well as to the investor. The Court, was concerned because it observed that the

Commission had not considered the essential factors upon which justness and reasonableness could be determined.

The Court held that it was essential to ascertain whether the investors had in fact recovered their investment in the abandoned property and the standby plant, and, if this investment had not been recovered, whether the rate of return allowed in the past and the historical earnings have compensated the investors for assuming the risk of obsolesence. Recognizing that such determinations must be made in the first instance by the Commission, the Court held that in the absence of findings made pursuant to an inquiry, it would be impossible to determine whether the rates meet the statutory standards of reasonableness and justness.

The Petitioners contend that in applying these standards, the Court below exceeded a proper scope of judicial review and imposed its judgment upon the Commission in contravention of the *Hope* case. This contention is wholly without merit.

The holding of the Court below that a finding as to a fair rate of return was necessary was predicated on the assumption that the prudent investment theory of rate regulation, purportedly adopted by the Commission, requires such a finding. That a finding of a fair rate of return is essential in the application of the prudent investment theory is too well established by the cases of this Court to permit any doubt. Mr. Justice Brandeis, in his dissenting opinion in *Missouri ex rel. Southwestern Telephone Company* v. *Public Service Commission,* 262 U.S. 276, 291, 67 L. Ed. 981, 986, specifically stated that the reasonableness of a rate under the prudent investment theory is dependent upon several subsidiary conclusions, one of which is the fair rate of return. Mr. Justice Brandeis also held that the measure of a fair rate of return depends, in part, upon the return required to attract capital to the enterprise. The Commission did not consider future conditions under which the proposed tariffs would be applicable with respect to their effect upon cost of capital or rate of return and made no basic findings on this subject.

The later cases of this Court have affirmed Mr. Justice Brandeis' holding as to the essentiality of a finding with respect to a fair rate of return in determining the reasonableness of rates under the prudent investment theory. *Colorado Interstate Gas Company* v. *Federal Power Commission, supra,* 605; *Panhandle Eastern Pipe Line Company* v. *Federal Power Commission,* 324 U. S. 635, 649-650, 89 L. Ed. 1241, 1251; *Federal Power Commission* v. *Hope Natural Gas Company, supra,* at 603; *Federal Power Commission* v. *Natural Gas Pipeline Co., supra,* at 596. The Opinions of this Court in both the *Hope* case at pages 603-605, and the *Natural Gas Pipeline* case, at pages 596-597, set out in detail the type of factual support required for determination of a fair rate of return. The record before the Commission was totally deficient of any evidence of this character.

Similarly, the requirement of the Court of Appeals that the record should contain evidence with respect to whether the investors actually had any unrecovered investment in West Plant and East Plant, and, if so, whether the historical earnings and rate of return allowed have compensated them for the risk of obsolescence of such properties, is inherent in the *Hope* doctrine. As this court has repeatedly said, the application of the prudent investment theory is designed to reflect a proper balance between the rights of investors and consumers. Since it is clear from the Commission's opinion that the reasonableness of the present rates was not predicated upon a consideration of these problems, the rates cannot be said to strike the balance between investors and consumers which is basic to a reasonable rate. If the investors have in the past been compensated for the risk of obsolescence, or if they presently have no unrecovered dollars in the property already abandoned, and to be abandoned, a rate designed to afford the investors additional payments with respect to these properties patently would be unfair. In the light of such of the history of the company as appeared in the record, the Court

of Appeals was of the opinion that the probabilities of unfairness in this area were so great as to require an inquiry into the problems. It is submitted that in this regard the Court below was logically carrying out the doctrines enunciated by this Court in the *Hope* case.

The Court below has had occasion in an earlier case, where it was challenged as substituting its judgment for that of a Commission, to amplify the view it has expressed in the present case. *Mississippi River Fuel Corp.* v. *Federal Power Commission,* 163 Fed. 2d 433. In that case the Court said at page 452:

> "Be that as it may, the Commission, even though expert, is forbidden to be arbitrary. And the courts are directed to prevent it from being so. The Commission cannot, and we do not understand it to claim that it can, shield arbitrariness by averments of its own infallibility, by technical expressions, or by failure to state adequate reasons for its conclusions. . . The Commission says that the court has substituted its judgment for that of the Commission. The Court has not done so. That contention in the present case is merely the recitation of a favorite cliche of administrative tribunals whose findings and conclusions have been queried by a court."

The Opinion of the Court below in the *Mississippi River* case is pertinent on the general problem involved in the present case of whether the action of the Court below constitutes a substitution of its judgment for that of the Commission, or is a proper exercise of its duty to require that findings of the Commission have adequate and proper evidentiary support. The following is taken from page 449 of that case:

> "The Commission cannot announce the applicability of a formula and then distort its application by failure to find accurately the factors required by the formula, or by departing from the essential progress of the formula from premise to conclusion. When the Commission announces principles or formulae as applicable

> the validity of its order can be determined only by measuring what it does against the principles it announces. This is so not only upon the authority of *Securities Comm'n* v. *Chenery Corp.*, but because any other course would permit an administrative agency to announce a proper principle and, under that protection, achieve an improper result by unrevealed considerations wholly apart from the announcement. The prescribed judicial review would be set wholly at naught by any such procedure. In so far as the Commission purported to act upon its own informed judgment, apart from formulae or general principles, its findings and reasons must be clearly and completely shown."

In the absence of findings and evidence with respect to a fair rate of return, the Petitioners contend that this deficiency is supplied by a prior rate proceeding in 1945. The Court below referred to earlier rate proceedings in which the factors relevant to a determination of a fair rate of return were considered, but held that such earlier considerations had no probative effect in the current case. It must be observed that, quite apart from the merits of the Petitioners contentions in this regard, the argument only points out that the Petitioners disagree with the view of the Court below on the question of substantial evidence. This court does not normally grant review for the purpose of determining whether the Court of Appeals is correct in its view that findings do not have the requisite evidentiary support.

It is submitted that the Court below properly rejected evidence in proceedings during the war years and under "sliding scale" regulation as determinative of what a fair rate of return should be in 1949. In support of the Court, it need only be pointed out that, between the date of the earlier cases and 1949, great changes occurred in the economic, financial, and regulatory background. The unregulated economy of 1949, which was adjusting itself to the changes in our national life brought about by the consequences of the war, was different from the controlled economy of the

war years. Factors affecting the cost of money similarly were different in the two periods, and the change of the company from a distributor of mixed gas to a distributor of straight natural gas also would have a bearing on the cost of its capital. Of equal if not greater significance is the fact that during the war years, the company's rates were determined on a sliding scale basis, which has substantial differences from normal rate regulation.

For these reasons, it is submitted that the Court below was correct in its holding that the prior proceedings were inadequate to supply the essential findings with respect to a fair rate of return.

3. The Court of Appeals Was Not Precluded from Considering the Rate of Return.

The petition of the Commission before this Court alleges in effect that Respondent failed to include in his petition for reconsideration before the Commission any specific objection to the inadequacy of the findings and record with respect to rate of return, the abandoned property and the standby plant. The Company, in its petition before this Court, is a bit more restrained, and makes this contention only with respect to the rate of return. It is contended that § 43-704 of the District Code, providing that no litigant may on appeal urge any ground not set forth in a petition for reconsideration filed with the Commission, precludes the Court of Appeals from deciding the appeal on grounds not preserved in a petition for reconsideration.

We believe the contention of Petitioners is without merit.

Respondent's petition for reconsideration is quite comprehensive (R. 135-145), and expressly raises the question of whether the investors have failed to recover the costs of the abandoned property. (R. 137-138). The Respondent in discussing the abandoned property, expressly referred to it as "so-called unrecovered cost of abandoned property". (R. 137). Moreover, the Respondent specifically set forth that the record fails to show that the company suffered net

losses in the past, or failed to earn a fair return, after giving effect to such loss as may have resulted from abandonment of the property. (R. 138). The petition also specifically states, "The evidence of record does not disclose the earnings of the company throughout the life of the property concerned." (R. 138). The petition further stated: (R. 138).

> "How can it be said 'that the exclusion of this item (unrecovered cost of abandoned property) from the rate base would deprive investors of a return on an investment originally made to furnish utility service', when the actual return of the company during the life of the property has not been determined?"

With respect to the issue of a fair rate of return, Respondent's petition for reconsideration specifically charged that "the rates approved are unreasonable and unjust to consumers, and would permit the company to earn an excessive rate of return." (R. 137). In amplification of this contention, the Respondent stated: (R. 139).

> "Only on the theory that stockholders assume the risks of losses under certain circumstances, such as result from a change in the art with resulting obsolescence, can a return of 6 percent or more to the utilities be justified. If such risks are to be removed, the return permitted should not exceed that realizable upon non-speculative high grade bonds."

In the light of these specific references in the Respondent's petition for reconsideration, it is clear that the issue of adequacy of return was adequately preserved. The determination of the adequacy of the findings to permit judicial review is clearly a matter of judical determination.

It must also be pointed out that a comprehensive petition for reconsideration was filed before the Commission on behalf of another litigant. (R. 155-161). That petition also sets forth the issues discussed in the Opinion of the Court below.

In addition to being in error on the facts, the Petitioners are also in error as to the applicable legal principles. The weakness of the contention is that it proves too much. If Petitioners are correct, the reviewing courts would be presented with the dilemma of being unable to set aside a patently unreasonable rate because a consumer litigant may not have specifically urged invalidating grounds, despite the statutory requirement that the rates be just and reasonable. It is the duty of the courts on review to protect against arbitrary administrative action and to make certain that the Commissions' conclusions as to the reasonableness of rates have a foundation in fact. Section 43-704 of the District of Columbia Code does not operate as a restriction on the power of the Court, but is a limitation directed to the litigants.

It is manifestly unsound to contend, as the Petitioners do, that the matter of a fair rate of return was not in issue. The question of a fair rate of return is always in issue in a rate proceeding. Moreover, that issue is also inherently part of the determination of rates under the prudent investment theory. Having adopted that theory, the Commission was under the obligation to take into consideration all the factors required by the formula; the reasoning must progress logically from premise to conclusion.

It is submitted that from the foregoing, it is clear that all the issues were properly before the Court of Appeals and that the court did not exceed its proper scope of review.

In considering Section 43-704 of the District of Columbia Code, it must be remembered that many of the orders of the Public Utilities Commission are issued without formal notice or hearing and a petition for reconsideration may be the first protest or reference to deficiencies therein. The present record on the contrary was quite extensive and all issues were the subject of evidence, argument or specific motion prior to the issuance of the final order.

Even if we were to assume, *arguendo,* that the issues were not properly before the Court, the Court would have power on its own motion to consider questions of law which were neither presented nor passed upon by the administrative agency in order to prevent a miscarriage of justice. *Hormel* v. *Helvering,* 312 U.S. 552, 557, 85 L. Ed. 1037, 1041. It is clear from that Opinion that the Court below was under the duty to review the case on all the issues involved even if there had been a failure on the part of Respondent to properly raise all the issues.

CONCLUSION.

The petitions present no issues requiring further review. The case is concerned with the fixing of local rates under a local statute, presents no constitutional or federal questions, and is not in conflict with decisions of this Court, or with decisions in any of the Circuits. In view of all of the foregoing, it is respectfully submitted that the petitions should be denied.

Respectfully submitted,

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APPENDIX.

D. C. Code, (1940) 43-301

"Every public utility doing business within the District of Columbia is required to furnish service and facilities reasonably safe and adequate and in all respects just and reasonable. The charge made by any such public utility for any facility or services furnished, or rendered, or to be furnished or rendered, shall be reasonable, just and non-discriminatory. Every unjust or reasonable or discriminatory charge for such facility or service is prohibited and is hereby declared unlawful. Every public utility is hereby required to obey the lawful orders of the commission created by this section."

D. C. Code, (1940) 43-704

"* * * Any public utility or any other person or corporation affected by any final order or decision of the commission may, within thirty days after the publication thereof, file with the commission an application in writing requesting a reconsideration of the matters involved, and stating specifically the errors claimed as grounds for such reconsideration. No public utility, or other person or corporation shall in any court urge or rely on any ground not so set forth in said application. The commission, within thirty days after the filing of such application, shall either grant or deny it. Failure by the commission to act upon such application within such period shall be deemed a denial thereof. If such application be granted, the commission, after giving notice thereof to all interested parties, shall, either with or without hearing, rescind, modify, or affirm its order or decision. The filing of such an application shall act as a stay upon the execution of the order or decision of the commission until the final action of the commission upon the application: *PROVIDED,* That upon written consent of the utility such order or decision shall not be stayed unless otherwise ordered by the commission. No appeal

shall lie from any order of the commission unless an application for reconsideration shall have been first made and determined."

D. C. Code, (1940) 43-706

"In the determination of any appeal from an order or decision of the commission the review by the court shall be limited to questions of law, including constitutional questions; and the findings of fact by the Commission shall be conclusive unless it shall appear that such findings of the Commission are unreasonable, arbitrary or capricious."